Court of Appeal File No. COA-24-CV-0468
Court File No. BK-21-02734090-0031

COURT OF APPEAL FOR ONTARIO

IN THE MATTER OF THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, c. B-3, as amended

IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF YG LIMITED PARTNERSHIP AND YSL RESIDENCES INC. OF THE CITY OF TORONTO, IN THE PROVINCE OF ONTARIO

BOOK OF AUTHORITIES OF THE APPELLANT KSV RESTRUCTURING INC. (IN ITS CAPACITY AS PROPOSAL TRUSTEE)

April 29, 2024

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INDEX

LIST OF AUTHORITIES

Tab	Case
22.	*Return on Innovation Capital Ltd. v. Gandi Innovations Ltd.*, 2011 ONSC 5018
23.	*Schnier v. Canada (Attorney General)*, 2016 ONCA 5
24.	*Syndic de Société de vélo en libre service*, 2023 QCCA 368
25.	*Trakopolis SaaS Corp. (2007996 Alberta Ltd.), Re*, 2020 ABQB 643
26.	*YG Limited Partnership (Re)*, 2022 ONSC 6138
27.	*YG Limited Partnership and YSL Residences (Re)*, 2021 ONSC 4178
28.	*YG Limited Partnership and YSL Residences (Re)*, 2021 ONSC 5206

Tab	Secondary Sources
29.	Standing Senate Committee on Banking, Trade and Commerce Report dated November 2003

TAB 1

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *0731431 B.C. Ltd. v. Panorama Parkview Homes Ltd.,* 2021 BCSC 607

Date: 20210401
Docket: S142529
Registry: Vancouver

Between:

0731431 B.C. Ltd., Daljit Singh Mattu, 0892995 B.C. Ltd., Rajpreet Singh Sangha, Grewal Management Ltd., and Jasprit Singh Grewal

Plaintiffs

And

Panorama Parkview Homes Ltd., 690174 B.C. Ltd., Jaswant Singh Sangha, Parmjit Kaur Sangha, Ranjit Singh Sangha, Svender Singh Sangha, Douglas William Wills and Balbir Kaur Dale, Crowe MacKay & Company Ltd. in its capacity as Trustee in Bankruptcy of Jaswant Singh Sangha, Panorama Parkview Homes Ltd. and 690174 B.C. Ltd.

Defendants

Docket: S151275
Registry: Vancouver

Between:

Daljit Singh Garcha and Jaswinder Kaur Garcha

Plaintiffs

And

690174 B.C. Ltd., Panorama Parkview Homes Ltd., Jaswant Singh Sangha, Parmjit Kaur Sangha, Raveen Sangha, Ranjit Singh Sangha, Svender Singh Sangha, Douglas William Wills, Balbir Kaur Dale, Grewal Management Ltd., Jasprit Singh Grewal and Crowe MacKay & Company Ltd. in its capacity as Trustee in Bankruptcy of Jaswant Singh Sangha, Panorama Parkview Homes Ltd. and 690174 B.C. Ltd.

Defendants

Docket: B150826
Registry: Vancouver

In the Matter of the Bankruptcy of Jaswant Singh Sangha

Docket: B160405
Registry: Vancouver

In the Matter of the Bankruptcy of Panorama Parkview Homes Ltd.

Docket: B160406
Registry: Vancouver

In the Matter of the Bankruptcy of 690174 B.C. Ltd

Before: The Honourable Mr. Justice Sewell

Reasons for Judgment

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Appearing on his own behalf:	Jaswant Singh Sangha
Appearing on their own behalf:	Douglas William Wills and Balbir Kaur Dale

No other appearances

Place and Date of Trial:	Vancouver, B.C. April 8 - 12, 15 - 18, 23 - 26, 29, 30, 2019, May 1-3, 2019, September 4 - 6, 9 - 13, 6-20, 23-27, 30, 2019, October 1-2, 2019, November 4,2019, December 2 - 6, 2019, January 13-17, 20 - 24, 27 - 31, 2020, February 3 - 7, 11, 2020, June 15-19, 22 - 26, 29, 30, 2020 and July 2 - 3, 2020
Place and Date of Judgment:	Vancouver, B.C. April 1, 2021

Table of Contents

Introduction

[1] These reasons address two civil actions (the "Civil Actions") and three appeals of notices of disallowance of bankruptcy claims (the "Bankruptcy Appeals") involving the parties to a successful subdivision project at the corner of 130th Street and 60th Avenue in Surrey, British Columbia (the "Project"). The ultimate question to be resolved is how the proceeds from the Project should be divided among the parties to these proceedings.

[2] Several of the parties have the last name "Sangha". To distinguish among them, I will refer to them by their first names after I have identified them. I intend no disrespect to any of them by so doing.

[3] The Project was conceived and managed by Jaswant Sangha ("Jaswant"), who is (i) a defendant in the Civil Actions; (ii) the bankrupt in one of the Bankruptcy Appeals; and (iii) the sole shareholder and director of two companies, 690174 B.C. Ltd. ("690174") and Panorama Parkview Homes Ltd. ("Panorama"), both of which are defendants in the Civil Actions as well as being the bankrupt companies in the other two Bankruptcy Appeals.

[4] Beginning in the 1990s, Jaswant became involved in acquiring, subdividing and selling properties located mostly in Surrey and other jurisdictions in the Fraser Valley. Jaswant usually involved other persons in the ownership of these projects. The evidence as to how the earlier projects were structured is incomplete. Some of the projects were profitable. Jaswant used the profits and the contacts he had made as a result of the earlier subdivisions to promote and pursue the Project.

[5] Jaswant began pursuing the Project in 2006. Ultimately, the Project produced a very significant profit. Despite this, Jaswant, 690174, and Panorama (the "Bankrupts") all ended up in bankruptcy (the "Bankruptcies"), in large part because of other businesses in which they were engaged.

[6] The legal and factual issues that must be addressed to determine the ultimate question of the rights of the parties to the Project's proceeds are complex and hotly disputed. The key underlying legal issues involve the nature of the relationships

created to develop the Project and the effect of the Bankruptcies on those relationships.

The Proceedings

[7] The proceedings before me are:

1. Vancouver Registry No. S151275 (the "Garcha Action"), in which Daljit Singh Garcha and Jaswinder Kaur Garcha (the "Garchas") are plaintiffs and Jaswant, 690174, Panorama, Parmjit Sangha ("Parmjit"), Raveen Sangha ("Raveen"), Ranjit Singh Sangha ("Ranjit"), Svender Singh Sangha ("Svender"), Douglas William Wills and Balbir Kaur Dale ("Wills and Dale"), Grewal Management Ltd. ("Grewal Management"), Jasprit Singh Grewal ("Mr. Grewal"), and Crowe MacKay & Company Ltd. in its capacity as Trustee in Bankruptcy of Jaswant Singh Sangha, Panorama Parkview Homes Ltd. and 690174 B.C. Ltd. (the "Trustee") are defendants;

2. Vancouver Registry No. S142529 (the "Grewal Action"), in which 0731431 B.C. Ltd. ("0731431"), Daljit Singh Mattu ("Mr. Mattu"), 0892995 B.C. Ltd. ("0892995"), Rajpreet Singh Sangha ("Rajpreet"), Grewal Management, and Mr. Grewal are plaintiffs and Panorama, 690174, Jaswant, Parmjit, Ranjit, Svender and the Trustee are defendants;

3. Vancouver Registry No. B150826 in the Matter of the Bankruptcy of Jaswant Singh Sangha (the "Jaswant Bankruptcy"), being appeals of notices of disallowance of proofs of claim filed by the plaintiffs in the Civil Actions in that bankruptcy;

4. Vancouver Registry No. B160406 in the Matter of the Bankruptcy of 690174 B.C. Ltd. (the "690174 Bankruptcy"), being appeals of notices of disallowance of proofs of claim filed in that bankruptcy by the same plaintiffs; and

5. Vancouver Registry No. B160405 in the Matter of the Bankruptcy of Panorama Parkview Holdings Ltd. (the "Panorama Bankruptcy"), being appeals of notices of disallowance of proofs of claim filed by the same

plaintiffs in that bankruptcy (proceedings 3 to 5 are referred to collectively as the "Bankruptcy Appeals").

The Joint Ventures

[8] The Project involved the acquisition of five contiguous lots, referred to in the evidence as Lots 1 to 5 (the "Lots"). The Lots were acquired over a period of several years and developed through a series of joint ventures, some of which were formalized through the execution of a corresponding written joint venture agreement ("JVA").

The written joint venture agreements

[9] The relevant written joint venture agreements are:

1. **2007 JVA** – an agreement dated October 5, 2007, between the Garchas, Onkar Malli and Manmeet Malli (the "Mallis"), Joginder Chahal, Malkait Bains, Harjinder Bassi, Gurcharan Singh Sandhu, Sarbjit Kaur Basraon and Balraj Basraon, Gurmit Singh and Manisha Sidhu, Sumit Sidhu, and 690174 (the "2007 Joint Venturers") to acquire and subdivide Lot 1 and to sell the subdivided lots created by that subdivision (the "2007 Joint Venture"). The 2007 JVA was amended in January 2010 to correct what appears to have been a clerical error in the original document.

2. **October 2010 JVA** – an agreement dated October 20, 2010, between 0892995 (a company owned by Rajpreet), 0731431 (a company owned by Mr. Mattu), and Panorama (the "October 2010 Joint Venturers") to acquire, build homes on, and sell lots created by the Project (the "October 2010 Joint Venture"). Although the numbered companies were the nominal parties to the October 2010 JVA, I find that the parties made no distinction between their personal dealings and dealings through their private companies with respect to the Project.

3. **November 2010 JVA** – an agreement dated November 15, 2010, to subdivide Lots 1 to 5 and sell the subdivided lots (the "November 2010 Joint Venture"). The parties to the November 2010 JVA were 690174,

Panorama, Jaswant, Wills and Dale, Parmjit, Ranjit, and Svender (the "November 2010 Joint Venturers").

4. **2011 JVA** – an agreement dated June 30, 2011, replacing the November 2010 JVA, whereby Grewal Management was added as a joint venturer to the November 2010 JVA (Grewal Management and the other parties to this agreement will be referred to as the "2011 Joint Venturers") to pursue the objects of the November 2010 Joint Venture (the **"**2011 Joint Venture").

The alleged oral joint venture agreements

[10] In addition to the written joint venture agreements, Grewal Management, Mr. Mattu, and Rajpreet allege that they entered into oral joint venture agreements with Jaswant pursuant to which they invested in the Project. Their position is that these oral joint venture agreements modified or superseded the terms of the written joint venture agreements.

The Parties

[11] Jaswant is the central figure in all of the matters before me. He was born and educated in India but has lived in Canada for many years. He is obviously astute in business. As the Trustee observed in his testimony, Jaswant had the ability to identify and develop properties that could be profitably subdivided.

[12] Jaswant is married to Parmjit. They have a daughter, Raveen. Raveen is the registered owner of the home in which Jaswant and Parmjit have lived for a number of years. Parmjit is a defendant in the Grewal Action and both Parmjit and Raveen are defendants in the Garcha Action.

[13] The Garchas are long-term residents of Surrey who got to know Jaswant and Parmjit through attending community events.

[14] Ranjit and Svender are Jaswant's brother and nephew.

[15] Wills and Dale are a married couple who were long-time family friends of Jaswant and Parmjit. Wills and Dale became involved in real estate projects being managed by Jaswant in the 1990s. They allege that they invested in those projects and that the proceeds of those previous investments were invested in the November 2010 Joint Venture.

[16] Mr. Grewal is the sole shareholder and director of Grewal Management. Although it is a member of the 2011 Joint Venture, Grewal Management alleges that its investment in the Project was made pursuant to an oral joint venture agreement made in June 2011 that entitled it to a greater share of the proceeds from the Project than is allocated to it in the 2011 JVA.

[17] Mr. Mattu was a long-time acquaintance of Jaswant's. He alleges that he invested in the Project through an oral joint venture agreement with Jaswant and his companies.

[18] Rajpreet was introduced to Jaswant by Mr. Mattu. He invested in the October 2010 Joint Venture through 0892995 and alleges he later agreed with Jaswant that this investment and an additional $600,000 he provided to Jaswant would be invested in the Project pursuant to an oral agreement similar to the one alleged by Mr. Mattu. He was initially represented by the same counsel as Mr. Grewal and Mr. Mattu. However, he filed a notice of intention to act in person in July 2019 and represented himself and 0892995 at trial thereafter.

[19] The Trustee is the Trustee in Bankruptcy of Jaswant, 690174, and Panorama, who has conducted a defence of the Garcha and Grewal Actions on their behalf.

Positions of the Parties

[20] In the Garcha Action, the Garchas seek an order that they are entitled to share in the proceeds from the Project by virtue of being the beneficial owners of an undivided 7/22 interest in Lot 1. The Garchas frame this claim both as a direct beneficial proprietary interest pursuant to the 2007 JVA and as a remedy for alleged breaches of fiduciary duty on the part of Jaswant and 690174 as managers of the 2007 Joint Venture's affairs. The Garchas' position is that the 2007 JVA is binding

and that it provides the basis for granting them a proprietary remedy against the proceeds of the Project. The Garchas also claim against the members of the 2011 Joint Venture based on knowing assistance of 690174's breaches of fiduciary duty and knowing receipt of property obtained from these breaches.

[21] The Trustee's position is that the 2007 JVA is binding and that 690174 initially held title to Lot 1 as bare trustee for the 2007 Joint Venturers, but that the trust came to an end due to subsequent events. The Trustee therefore argues that the rights of the 2007 Joint Venturers to receive profits from the 2007 Joint Venture are purely contractual.

[22] The Grewal plaintiffs conceded at trial that the 2007 JVA was binding, but took the position that it did not create any trust in favour of the Garchas over the proceeds of the Project.

[23] In the Grewal Action, Mr. Grewal, Mr. Mattu, Rajpreet, and their respective companies seek orders that they are entitled to constructive trusts over the net proceeds of sale of the subdivided lots created by the Project. They allege that they made direct financial contributions to the costs of the Project pursuant to oral joint venture agreements with Jaswant stipulating that their financial contributions would entitle them to a proprietary interest the Project.

[24] Rajpreet also bases his claim to a constructive trust on alleged breaches of fiduciary duty by Jaswant and Panorama with respect to funds Rajpreet and 0892995 provided to them pursuant to the October 2010 JVA.

[25] In the Bankruptcy Appeals, the plaintiffs in the Civil Actions seek to set aside the Trustee's disallowances of the claims they filed in the Bankruptcies. They rely on the same grounds advanced in the Civil Actions, arguing that their interests in the Project do not form part of the bankrupt estates' assets divisible among their creditors and that they are not equity claims. Their position is that the issues raised in the Bankruptcy Appeals should be decided *de novo* in these proceedings.

[26] In all proceedings, the Trustee takes the position that the claims of the plaintiffs are equity claims as defined in the *Bankruptcy and Insolvency Act*, R.S.C.

1985, c. B-3 [*BIA*], and are therefore postponed to the claims of all other creditors of the Bankrupts pursuant to s. 140.1 of the *BIA*. The Trustee says there are insufficient funds remaining in the bankrupt estates to satisfy prior ranking claims and that any claims that the plaintiffs can establish are therefore moot.

[27] In all proceedings, the defendants take the position that the plaintiffs have not established any claim to equitable relief by way of a constructive trust or otherwise, and that the net proceeds of the Project should be distributed in accordance with the terms of the 2011 JVA.

[28] For the reasons that follow I have decided that the plaintiffs' claims are not equity claims as defined in the *BIA*, and that the Garchas, Mr. Mattu, Rajpreet, and their companies are entitled to equitable remedies with respect to the proceeds of sale of the subdivided lots. However, I find that the claim of Mr. Grewal and Grewal Management must be dismissed except insofar as Grewal Management is entitled to its share of the net proceeds of the 2011 Joint Venture.

[29] In these reasons I will first deal with a number of procedural issues. I will then address the credibility of the witnesses and make findings of fact, following which I will consider the claims advanced by the plaintiffs.

Procedural History

[30] This trial results from four orders of Justice Bowden, who was previously the case management judge in all of these proceedings. Two of the orders are dated November 15, 2017, while the other two are dated January 29, 2018, and June 26, 2018. The reasons for each of these orders were published and are indexed as 2017 BCSC 2064, 2017 BCSC 2071, 2018 BCSC 137, and 2018 BCSC 1049, respectively.

[31] In the reasons indexed as 2017 BCSC 2064, Justice Bowden addressed the Grewal plaintiffs' application for a declaration that the automatic stay of proceedings against 690714 and Panorama as bankrupts provided for in the *BIA* no longer applied to the Grewal Action. Justice Bowden reviewed the procedural history of this matter up to that date and noted that on April 8, 2016, Justice Kirkpatrick of the

Court of Appeal had ordered, by consent, that the stay of proceedings against Jaswant pursuant to his bankruptcy be lifted on certain terms. Justice Bowden found as a fact that the Trustee had, at that time, also consented to an order lifting the automatic stay of proceedings against 690174 and Panorama to permit the Grewal plaintiffs to proceed with the Grewal Action.

[32] The Trustee did not deny that he had made such an agreement. However, he argued that by the end of July 2016 he had determined that the Garcha and Grewal claims were equity claims, and that the inspectors of the bankrupt corporations had authorized him to take steps to maintain the stay of proceedings in the actions against those corporations.

[33] Justice Bowden did not accept the Trustee's submissions and made a declaration pursuant to s. 69.4 of the *BIA* that the stay of proceedings no longer applied to the Grewal Action, subject to a requirement that if judgment was obtained against either corporation, no steps to enforce the judgment could be taken without leave of the Court. In addition, he confirmed the authority of the Trustee to defend the action, as authorized by a resolution of the inspectors of the Bankrupts dated September 1, 2016.

[34] In the reasons indexed as 2017 BCSC 2071, Justice Bowden granted a declaration that the automatic stay of proceedings no longer applied to the Garcha Action. Because there was no express agreement on the part of the Trustee to the lifting of the stay of the Garcha Action, Justice Bowden applied the factors set out in *Re Advocate Mines Ltd.* (1984), 52 C.B.R. (N.S.) 277 (Ont. S.C.J.), and determined that the Garchas had met the applicable test for lifting the stay of their action.

[35] In the reasons indexed as 2018 BCSC 137, Justice Bowden addressed the procedural issues that arose from the fact that the Grewal and Garcha plaintiffs had also filed proofs of claim with the Trustee, which the Trustee had disallowed or ruled were equity claims. He permitted the Bankruptcy Appeals to continue with respect to the claims of creditors other than the Garcha and Grewal plaintiffs and gave leave to the Trustee to apply for a distribution of funds held in trust on the completion of those appeals. He also permitted the Civil Actions to proceed and directed that they

be heard at the same time as the Bankruptcy Appeals. Finally, he directed that the procedures set out in the *Supreme Court Civil Rules,* B.C. Reg. 168/2009 [*SCCR*], would apply to the contemporaneous hearings of the trials in the Civil Actions and the Bankruptcy Appeals.

[36] In the reasons indexed as 2018 BCSC 1049, Justice Bowden gave the Trustee leave to participate in the Civil Actions by being added as a defendant. He ordered the Grewal and Garcha plaintiffs to amend their notices of civil claim to add the Trustee and gave leave to the Trustee to file responses for Jaswant, 690174, and Panorama. In addition, he reiterated that the Civil Actions and the Bankruptcy Appeals should be heard at the same time and be subject to the *SCCR.* Justice Bowden also ordered that the issues raised in the Civil Actions must be decided *de novo*, and that to the extent that those decisions are inconsistent with the Trustee's decisions in the notices of disallowance, the Court's decisions will prevail.

[37] Based on the foregoing, I am satisfied that Justice Bowden decided that all issues raised in the Civil Actions and the Bankruptcy Appeals should be decided *de novo* pursuant to the procedures for actions set out in the *SCCR.*

[38] No appeal was taken from Justice Bowden's orders.

[39] I have also independently concluded that these proceedings fall into that category of bankruptcy cases in which the interests of justice require that the issues be determined by a trial before the court. Although the general rule is that appeals from a Trustee's disallowance of claims are true appeals, the direct conflict in the evidence of the parties and the difficult and complicated legal issues raised in the proceedings require that the court determine the issues *de novo* on the basis of evidence presented at trial.

[40] In *Credifinance Securities Limited v. DSLC Capital Corp.,* 2011 ONCA 160, the Ontario Court of Appeal recognized that there will be cases that are simply not suitable to be decided pursuant to the summary provisions of the *BIA* and that on appeal the court has jurisdiction to determine the issues *de novo* if required in the interests of justice. In my view this is one of those cases. I note that the issues

raised in these proceedings raise complex factual and legal issues and require credibility findings with respect to conflicts in the evidence. As such, they were not suitable for summary disposition.

[41] As indicated, the Trustee filed responses to civil claim in the Civil Actions and fully participated as an adverse party in the actions and throughout the trial. I also note that counsel for the Trustee indicated in argument that the Trustee was seeking a resolution of all issues before me.

[42] In these circumstances I conclude that it would be unfair to the Garcha and Grewal plaintiffs to give deference to the Trustee's factual conclusions on these issues. I am also satisfied that the Trustee has made legal errors that would have led to the allowance of the Bankruptcy Appeals on a true appeal.

[43] I will therefore proceed to determine the issues raised in the Civil Actions *de novo* on the record before me and apply those determinations to decide the outcome of the Bankruptcy Appeals. This will make it unnecessary for me to consider the Bankruptcy Appeals separately.

Credibility

[44] I do not find it necessary to determine all of the credibility issues raised by the parties in their submissions. However, there are a number of credibility findings that I must make at the outset to determine the relevant facts.

[45] The considerations to be taken into account in assessing credibility were reviewed in *Bradshaw v. Stenner*, 2010 BCSC 1398:

> [186] Credibility involves an assessment of the trustworthiness of a witness' testimony based upon the veracity or sincerity of a witness and the accuracy of the evidence that the witness provides (*Raymond v. Bosanquet (Township)* (1919), 1919 CanLII 11 (SCC), 59 S.C.R. 452, 50 D.L.R. 560 (S.C.C.)). The art of assessment involves examination of various factors such as the ability and opportunity to observe events, the firmness of his memory, the ability to resist the influence of interest to modify his recollection, whether the witness' evidence harmonizes with independent evidence that has been accepted, whether the witness changes his testimony during direct and cross-examination, whether the witness' testimony seems unreasonable, impossible, or unlikely, whether a witness has a motive to lie, and the demeanour of a witness generally (*Wallace v. Davis*, [1926] 31 O.W.N. 202

> (Ont.H.C.); *Faryna v. Chorny*, 1951 CanLII 252 (BC CA), [1952] 2 D.L.R. 354 (B.C.C.A.) [*Farnya*]; *R. v. S.(R.D.),* 1997 CanLII 324 (SCC), [1997] 3 S.C.R. 484 at para.128 (S.C.C.)). Ultimately, the validity of the evidence depends on whether the evidence is consistent with the probabilities affecting the case as a whole and shown to be in existence at the time (*Farnya* at para. 356).
>
> [187] It has been suggested that a methodology to adopt is to first consider the testimony of a witness on a 'stand alone' basis, followed by an analysis of whether the witness' story is inherently believable. Then, if the witness testimony has survived relatively intact, the testimony should be evaluated based upon the consistency with other witnesses and with documentary evidence. The testimony of non-party, disinterested witnesses may provide a reliable yardstick for comparison. Finally, the court should determine which version of events is the most consistent with the "preponderance of probabilities which a practical and informed person would readily recognize as reasonable in that place and in those conditions" (*Overseas Investments (1986) Ltd. v. Cornwall Developments Ltd. (1993)*, 1993 CanLII 7140 (AB QB), 12 Alta. L.R. (3d) 298 at para. 13 (Alta. Q.B.)). I have found this approach useful.

[46] The most important credibility issue in these proceedings is the extent to which I can rely on Jaswant's oral evidence.

[47] In carrying out his analysis of the Project, the Trustee placed considerable reliance on the information and explanations that Jaswant provided to him. This led the Trustee to conclude that Jaswant was a generally honest debtor whose financial difficulties arose from being undercapitalized and from the general economic conditions created by the 2008 financial crisis.

[48] However, I have come to a different conclusion. I found Jaswant to be a most unsatisfactory witness. His evidence was self-serving, lacked candour, and was in many instances self-contradictory. He also tended to be argumentative rather than answering questions directly. At times he professed to have no memory of events relating to the Project. However, at other times he emphatically testified to events that favoured his position. I also note that he repeatedly testified while being cross-examined by parties adverse to his interests he had no independent memory of events and was almost entirely reliant on documents to answer questions put to him. However, his memory was better when he was cross-examined by counsel for his wife and counsel for the Trustee, who were aligned with him at trial but were entitled to cross-examine him because he was called to testify as an adverse party pursuant to Rule 12-5(20) of the *SCCR*.

[49] In addition, on more than one occasion Jaswant contradicted his previous evidence or the evidence he had given in examination for discovery. As was the case with many of the defendants, when confronted with the inconsistencies in his evidence Jaswant testified that he had been under a lot of stress and was taking medications when he gave his previous evidence. However, he made no attempt to correct any answers given on his previous examinations until confronted with the contradictions at trial, and he did not provide any medical evidence supporting his assertion that his memory had been affected by medications.

[50] In assessing Jaswant's credibility, I also take into account some of his conduct during the Project and in the course of the Bankruptcies that casts doubt on his trustworthiness.

[51] In cross-examination, Jaswant acknowledged as accurate the contents of a letter dated March 12, 2012, addressed to him from Royal Morton, a lawyer at Buckley Hogan. Mr. Morton represented Jaswant in an action brought by Hardeep Singh Gill ("Hardeep Gill") against 690174 with respect to a failed real estate transaction, which I will describe later. Jaswant and 690174 waived solicitor-client privilege over the contents of this letter, and it was admitted into evidence at trial.

[52] In this letter, Mr. Morton confirmed that Jaswant did not wish the other 2007 Joint Venturers to be informed of his post-2007 dealings with Hardeep Gill. Hardeep Gill had obtained a large judgment (the "Gill Judgment") against 690174 in the aforementioned action and registered the judgment against Lot 1, the subject of the 2007 JVA, in the New Westminster Land Title Office.

[53] Jaswant expressed concerns to Mr. Morton about disclosing this fact and other aspects of his financial and legal affairs to the 2007 Joint Venturers. He said that he would look bad within his community if Mr. Morton approached them to obtain affidavits to support Jaswant's evidence that 690174 beneficially owned only 1/23 of the proposed lots to be subdivided from Lot 1 and that the balance of the lots was beneficially owned by the other 2007 Joint Venturers.

[54] This conduct revealed a marked lack of candour on Jaswant's part. It also put the beneficial ownership interests of the 2007 Joint Venturers in Lot 1 at risk by denying them the opportunity to intervene to protect their position with respect to the Gill Judgment.

[55] In addition, Jaswant admitted that he prepared what he knew to be fabricated promissory notes which were certified to be true by Raveen and Parmjit in proofs of claim they filed in the Bankruptcies.

[56] In the 690174 Bankruptcy, Parmjit filed a claim as an ordinary creditor in the amount of $699,590.08, which she certified was based on promissory notes purportedly made on March 31, 2009, for $132,000, and January 1, 2010, for $319,338.55. Both notes provided for interest at 7% per month, which I accept was meant to be 7% per annum. Jaswant executed the notes on behalf of 690174. However, in cross-examination at trial, Jaswant and Parmjit admitted that Jaswant had prepared these notes after 690174 was assigned into bankruptcy on April 21, 2016, and backdated them.

[57] In the Jaswant Bankruptcy, Parmjit swore an affidavit stating that she had contributed one-third of the amount advanced from a joint account in the names of Jaswant, Parmjit, and Raveen as a loan to 690174, and that Jaswant had agreed to guarantee that loan.

[58] However, Parmjit and Jaswant's evidence at trial was that Parmjit had invested these sums in the Project on her own behalf. When cross-examined on this discrepancy and on the dates of the promissory notes, Parmjit described the promissory notes as having been prepared by mistake and stated that she no longer relied on them.

[59] Jaswant prepared similar promissory notes payable by 690174 to Raveen's company, 688350 B.C. Ltd. ("688350"), purportedly dated March 31, 2009, and December 30, 2006. 688350 filed a proof of claim in the 690174 Bankruptcy for principal and interest on those notes to the date of bankruptcy. At trial, Raveen and

Jaswant admitted that these notes had not been prepared until after 690174 had been assigned into bankruptcy.

[60] In my view these documents were an attempt to defraud the creditors of the bankrupt estates. I do not accept the explanations given by Parmjit and Raveen for the creation of these documents. In effect, they testified that they did not understand the process of making a claim in bankruptcy and did not understand the documents that they certified or affirmed. I find that this explanation lacks credibility.

[61] I therefore do not find Jaswant, Parmjit, or Raveen to be witnesses whose evidence I can accept without corroboration.

[62] I found the evidence of the plaintiffs and other defendants generally to be credible, unless I indicate otherwise in the course of these reasons. However, I do recognize that the reliability of all of the oral evidence in this case is affected by the long period of time that has elapsed between the time of the events testified to and the trial. Most of the critical events in this case occurred eight to 15 years before the trial. In addition, I suspect that at times all witnesses were filling in gaps in their memories and were in some instances influenced by what they wanted to remember rather than their actual recollections.

[63] These concerns require me to rely principally on the documentary evidence and on inferences from established facts in making the findings of fact necessary to resolve the issues before me.

Findings of Fact and Chronology of Events

[64] The parties filed an Agreed Statement of Facts at trial. It is neither necessary nor possible to incorporate all of its details in these reasons. Because there is considerable disagreement about the nature of the relationships between the parties and the agreements they made, I will make additional findings of fact necessary to decide those issues in the following chronology of events.

Purchase of Lot 1 and the 2007 JVA

[65] In the 2000s, Jaswant promoted the three land assembly and subdivision developments that are most relevant to these proceedings. Two of the developments were referred to in the evidence as Sangha Groups 1 and 2, and involved the assembly and subdivision of residential lots in Surrey, B.C. The Project was the third development. Jaswant began to pursue the Project at the same time as Sangha Group 2, in or about 2006.

[66] On April 14, 2006, 688350 entered into an agreement with the owners of 13020 60th Ave. to purchase that property, which is referred to throughout these reasons as Lot 1, for $2,700,000. The purchase price was increased to $2,725,000 in subsequent agreements that extended the closing date for its purchase.

[67] Around this time, Jaswant had discussions with the plaintiff Daljit Singh Garcha about investing in real estate. The evidence of Mr. Garcha and Jaswant about the content of these discussions is to some extent contradictory. Mr. Garcha testified that Jaswant told him that he was working to acquire and subdivide Lot 1, and that if he and his wife Jaswinder Kaur Garcha were willing to invest, they could obtain title to seven of the lots to be created from the subdivision of Lot 1 for an investment of approximately $50,000 to $60,000 per lot. It was unclear whether these amounts were in addition to the initial contribution made by the Garchas.

[68] Jaswant's evidence is that he told Mr. Garcha that Lot 1 was to be part of a larger land assembly and subdivision and that the Garchas would receive a proportionate share of the net profits from the sale of the lots to be subdivided from Lot 1. Mr. Garcha denies that Jaswant told him this. I prefer Mr. Garcha's evidence on the issue of whether he was told that Lot 1 was to be part of a larger land assembly. I note that Jaswant's evidence on this issue is inconsistent with his desire expressed to Mr. Morton not to inform the members of the 2007 Joint Venture of his dealings with respect to Lot 1. However, I have concluded that these discussions did not determine the nature of the legal relationship that would pursue the object of subdividing Lot 1. I conclude that in these discussions Mr. Garcha and Jaswant were discussing the general business terms of Jaswant's proposal, but that it was

understood there would be a written document executed that set out their agreement.

[69] As a result of these discussions, the Garchas advanced $150,000 to 688350 on December 28, 2006, and $242,000 to 690174 on March 30, 2007. I find that these funds were used to provide part of the amount due on closing of the purchase of Lot 1 and that Jaswant gave instructions to the Garchas to pay the $150,000 to 688350, telling them that the funds would be used to help pay for the purchase of Lot 1. I also find that the funds the Garchas provided to 690714 and 688350 were provided for the express purpose of acquiring Lot 1.

[70] In addition, it is agreed that other members of what became the 2007 Joint Venture contributed to the purchase of Lot 1. The Mallis advanced $392,000 to 690174 through their company, Joginder Chahal advanced $100,000, and Malkait Bains advanced $56,000. Other members of the 2007 Joint Venture contributed lesser amounts.

[71] 688350 assigned its interest pursuant to the agreement to purchase Lot 1 to 690174, which completed the purchase on April 2, 2007, thereby becoming the registered owner of that lot. I find that 688350 acted as 690174's agent in all respects with regard to the acquisition of Lot 1.

[72] There was considerable evidence led with respect to the amount that 690174 paid to 688350 to obtain the assignment of the agreement to purchase Lot 1. The assignment agreement contemplated that 690174 would pay 688350 an assignment fee of $292,000 in addition to the amount that 688350 was required to pay for Lot 1. 690174 did pay $292,000 to 688350, but almost immediately thereafter 688350 transferred $300,000 to 690174. In the result, these amounts netted out. I find that 688350 did not in fact receive any assignment fee. It is likely that the purpose of the assignment fee was to increase the apparent amount that was paid to acquire Lot 1 to assist in maximizing mortgage financing in aid of the purchase.

[73] By April 2, 2007, the investors in Lot 1 had provided all of the payments outlined above. The funds necessary to purchase Lot 1 were provided by: (i) the

deposit; (ii) a payment from 690174's solicitors, Buckley Hogan, in the amount of $895,724.05; (iii) an official cheque for $25,000; and (iv) mortgage proceeds from a mortgage in favour of IMOR Capital of $1,607,037.96 (the "IMOR Mortgage"). The cash portion of the purchase price was less than the total of the amount received from the persons who became members of the 2007 Joint Venture.

[74] On October 5, 2007, the Garchas, the Mallis, Joginder Chahal, Malkait Bains, Harjinder Bassi, Gurcharan Singh Sandhu, Sarbjit Kaur Basraon and Balraj Basraon, Gurmit Singh and Manisha Sidhu, Sumit Sidhu, and 690174 executed the 2007 JVA.

[75] The effect and scope of the 2007 JVA is very much in dispute in these proceedings. I will address its interpretation later in these reasons.

[76] The following provisions of the 2007 JVA are relevant:

1. Recital B states that the parties have agreed to form the 2007 Joint Venture for the purpose of investing in Lot 1, subdividing it into approximately 22 RF-9 residential lots, and selling the lots.

2. Recital C states that 690174 shall hold legal title to Lot 1 and develop it as bare trustee on behalf of the 2007 Joint Venture.

3. Paragraph 2.2 provides that 690174 acknowledges and agrees that it is holding 20 lots in trust for the 2007 Joint Venturers as bare trustee and that the 2007 Joint Venturers are each beneficial owners of those lots in the ratio of their proportionate shares. The reference to 20 lots appears to have been an error that was corrected to 22 lots in a later amendment executed for that purpose.

4. Paragraph 4.2 provides that the 2007 Joint Venturers each own as tenants in common, as their separate property, an undivided beneficial interest in the Project (defined as the development of Lot 1) and the 2007 Joint Venture assets in the ratio of their respective proportionate shares. To avoid confusion with the Project as defined in paragraph 1 of these

reasons, I will refer to the Project defined in the 2007 JVA as the Lot 1 Project.

5. Paragraph 6.2 provides that Jaswant Sangha be engaged as manager of the Lot 1 Project on terms acceptable to the management committee.

6. Paragraph 8.1 provides for the distribution of all revenue received relating to the Lot 1 Project, firstly to pay secured creditors of the Lot 1 Project, secondly to pay all unsecured claims against the Lot 1 Project, and thirdly to distribute the net proceeds to the 2007 Joint Venturers in accordance with their proportionate shares.

[77] The agreement also contained detailed provisions for funding of Lot 1 Project expenses and remedies on default.

[78] I find that although the 2007 JVA was dated six months after the acquisition of Lot 1, it was at all times agreed that the terms under which Lot 1 would be acquired and developed would be set out in a written agreement and that the rights and obligations of the parties with respect to Lot 1 would be and are governed by the terms of the 2007 JVA.

[79] I find that Jaswant and 690174 undertook responsibility for the management of the Lot 1 Project. From the outset, Jaswant made all decisions with respect to the development of Lot 1 without consulting with the other 2007 Joint Venturers or obtaining any prior approval for his decisions, even though the terms of the 2007 JVA required authorizations to make major decisions about the Lot 1 Project.

[80] The IMOR Mortgage required payment of interest at a high rate. Jaswant negotiated two further mortgages over Lot 1 to replace the IMOR financing. The first replacement mortgage was registered on November 1, 2007, in favour of Pacific Coast Mortgage Investment Corporation (“PMIC”). The Garchas executed this mortgage as covenantors on or about October 3, 2007. This mortgage was also secured by what would become known as Lot 2, one of the other lots assembled for the Project, and by a mortgage granted by the Mallis over their home.

[81] This mortgage was in turn replaced by a mortgage to PMIC registered on July 7, 2009, which was also secured by Lot 2, a half interest in the Mallis' home, and the home in which Jaswant and Parmjit lived. Although she did not live there, Raveen was the registered owner of the property on which Jaswant and Parmjit resided, and she was accordingly required to execute that mortgage. The Garchas executed this mortgage as covenantors, thereby assuming personal responsibility for its repayment, as they had with the two previous mortgages.

[82] Paragraph 2.2 of the 2007 JVA was amended in January 2010 to make it clear that the Joint Venture participants other than 690174 were entitled to a proportionate share of 22 lots, not 20 lots as previously stated. The 2010 amendment, which was executed by 690174, repeated that 690174 held legal title to Lot 1 as bare trustee on behalf of the 2007 Joint Venturers.

Purchase of Lots 2 to 4 and the November 2010 JVA

[83] Jaswant arranged the purchase of 3 additional lots (Lots 2 to 4) between 2007 and 2010.

[84] On August 22, 2006, 688350 contracted to purchase what became Lot 2 for $1,250,000. The agreement required a deposit of $150,000 within 48 hours of subject removal and was to complete on March 31, 2007. This deposit was paid by 688350 on or about December 6, 2006.

[85] On April 27, 2007, 690174 transferred $300,000 into the account of Parkwood Developments, an entity apparently associated with the defendant Ranjit. On April 30, 2007, 690174 advanced $27,886.96 to its solicitors, Buckley Hogan, and Ranjit advanced $345,000 from the Parkwood Developments account to Buckley Hogan to acquire Lot 2. The balance of the purchase price was paid from the proceeds of a mortgage in favour of TD Canada Trust in the amount of $750,000.

[86] The purchase of Lot 2 closed on April 30, 2007, when a transfer of one undivided half interest to Jaswant and Parmjit as joint tenants and the other half interest to Ranjit and Svender as joint tenants was registered. No documentation was put in evidence with respect to the transfer of the purchase agreement from

688350 to the ultimate purchasers. As with Lot 1, I am satisfied that 688350 acted on behalf of and at the direction of Jaswant in all of its dealings with Lot 2.

[87] On August 4, 2007, 690174 made an agreement to purchase what came to be known as Lot 3 for $1,350,000. 690174 paid the required deposit of $225,000 in four installments between August 7, 2007, and March 7, 2008. On March 12, 2008, 690174 assigned the purchase contract to Jaswant. On June 23, 2008, 690174 advanced a total of $211,490.70 to Buckley Hogan towards the purchase of the lot.

[88] The purchase of Lot 3 completed on June 23, 2008, when title was transferred into the names of Jaswant and Parmjit as joint tenants. The funds necessary to pay the purchase price came from the advances made by 690174 described in the preceding paragraph and from the proceeds of a mortgage in favour of the Royal Bank of Canada in the principal amount of $945,000.

[89] On March 11, 2008, Jaswant made an agreement to purchase what became known as Lot 4 for $1,445,000. 690174 paid the required deposit of $100,000 by an official cheque that had been issued on February 16, 2008. On August 4, 2008, 690174 advanced $388,227.53 to Buckley Hogan to pay part of the purchase price for the lot. On August 8, 2008, title to Lot 4 was transferred into the names of Wills and Dale as joint tenants as to a half interest and Jaswant as to the other half interest. The balance of the purchase price above the funds provided by 690174 came from the proceeds of a mortgage in favour of Gulf & Fraser Fisherman’s Credit Union in the amount of $994,196.25. Wills and Dale gave their covenants to pay this mortgage, which of course charged their registered interest in Lot 4.

[90] By 2010, Jaswant had organized the acquisition of Lots 1 to 4 and had reached an agreement with the owner of an additional lot (Lot 5), Satgur Investments Ltd. (“Satgur”), to contribute that lot to the Project and participate in the Project as a joint venturer. At some point, a draft joint venture agreement was prepared which included Satgur as a participant, but later, probably in the summer of 2010, Satgur decided not to participate.

[91] On November 15, 2010, 690174, Panorama, Jaswant, Wills and Dale, Parmjit, Ranjit, and Svender executed the November 2010 JVA.

[92] The terms of the November 2010 JVA were very similar to those of the 2007 JVA. Paragraph 4.1 sets out the proportionate shares of the November 2010 Joint Venturers in the Project. By the express terms of the November 2010 JVA, each November 2010 Joint Venturer became the beneficial owner of its proportionate share of all of the Lots involved in the Project. Paragraph 4.2 of the November 2010 JVA is identical to paragraph 4.2 of the 2007 JVA, reading as follows:

> 4.2 The Joint Venturers each own as tenants-in-common, as their separate property, an undivided beneficial interest in the Project and the Joint Venture Assets in the ratio of their respective Proportionate Shares.

[93] I will refer to the mortgages taken out to purchase Lots 1 to 5 as each of the "Acquisition Mortgages". Lots 1 and 5 were each approximately twice as large as the other three lots. Accordingly, they were considerably more expensive to acquire.

Project financing

[94] It is quite clear from the evidence that the Project was undercapitalized from the outset and that Jaswant needed investors to pursue it. This problem continued throughout the Project, but arose most frequently when Jaswant needed funds to close on the purchase of each of the 5 Lots, and later when charges were registered in the New Westminster Land Title Office against title to some of the Lots.

[95] In the preceding paragraphs I outlined how funds flowed to purchase Lots 1 to 4. However, the evidence with respect to the actual source of the funding, with the exception of Lot 1, is incomplete and confusing. The Trustee prepared a number of schedules with respect to the financing of the acquisition of Lots 2 to 4. Unfortunately, those schedules are of limited utility because they do not show the source of the funds used by the purchasers of the Lots. For example, the Trustee stated that 690174 contributed all of the funds for the down payment required to purchase Lots 3 and 4 because they were paid out of 690174's bank account. However, a significant portion of these funds were said to be profits from Sangha Groups 1 and 2, and there is evidence, which I will refer to later, indicating that

$500,000 of the proceeds from Sangha Group 2 had previously been assigned to Mr. Mattu as an investment in the Project.

[96] Similarly, in Schedule 1 to the Trustee's Ninth Report, prepared at my request, the Trustee credited Panorama with contributing $729,936.70 to the acquisition of Lot 5, consisting of the $300,000 deposit paid on the purchase price and $428,936.70 provided at closing. However, the evidence is clear that $200,000 of the deposit came from funds provided by 0892995 and the balance came from deposits paid directly to Panorama from purchasers of lots to be created from the ultimate subdivision of the Project. Panorama had no right to use those deposits for its own benefit because they were by that time the property of the November 2010 Joint Venture. I have no difficulty in finding that Panorama contributed at most $100,000 of its own funds to the purchase of Lot 5.

[97] In addition, it is difficult to reconcile the amounts that the Trustee credited to 690174 as contributions to the Project with the Trustee's conclusion in his Preliminary Report that the net amount, after repayments, of Sangha family contributions to 690174 and Panorama from the Sangha family joint account was only $63,365. While this calculation does not take into account contributions from Sangha Groups 1 and 2, there still remains great uncertainty as to the actual net amount of Sangha family contributions to the Project.

Acquisition of Lot 5 and the 2011 JVA

[98] As stated above, it was originally contemplated that Satgur would participate in the Project by contributing Lot 5, which it owned, in exchange for a 28.5% proportionate share. However, at some point in 2010 Satgur withdrew from the Project.

[99] This meant that the Project required additional funds to remain viable and, in particular, to purchase Lot 5 from Satgur. Although scant attention was paid to Satgur's withdrawal in the evidence, it obviously put further financial pressure on the Project. Lot 5 was one of the two larger Lots and was of vital importance to the

Project. Instead of Satgur providing Lot 5 as its contribution to the Project, Jaswant was forced to find additional capital to purchase it.

[100] The November 2010 JVA contemplated Panorama's acquisition of Lot 5 and its utilization in the Project. However, I find that from 2010 to 2011, Jaswant and Panorama lacked the funds necessary to complete its purchase.

[101] On August 20, 2010, Panorama entered into an agreement with Satgur to purchase Lot 5 for $3,300,000. Although it was not expressly set out in the evidence, it appears that Panorama was incorporated to purchase Lot 5. The purchase agreement required Panorama to provide a deposit of $300,000 by August 30, 2010. I find that Jaswant did not have sufficient funds to pay the deposit on that date. However, he was able to extend the payment date to November 17, 2010.

[102] Panorama's lack of funds also resulted in extensions of the closing date for the purchase of Lot 5. On April 5, 2011, Satgur and Panorama agreed to extend the completion date to June 30, 2011.

[103] In or before June 2010, Jaswant began to sell and receive deposits from persons who signed agreements to purchase lots that were to be subdivided from the Project. Most of these agreements showed Panorama as the seller. Instead of holding the deposits in trust, Panorama used them as part of the funds required to complete the purchase of Lot 5. By June 30, 2011, Panorama had deposited $516,000 in presale deposits into its Coast Capital Savings Account, which it provided to Buckley Hogan to partially fund the purchase.

[104] In June 2011, Jaswant asked Mr. Mattu to assist him in finding the additional funds necessary to complete the purchase of Lot 5. Mr. Mattu then introduced Jaswant to the plaintiff Jasprit Grewal.

[105] After some discussion, Mr. Grewal agreed to invest in the Project, utilizing his company, Grewal Management. Mr. Grewal's counsel summarized his evidence about his discussions with Jaswant as follows:

> Mr. Grewal described the meeting at Lot 1, at which Mr. Sangha indicated the neighboring lot, Lot 5, had to be purchased for the Project and that he and his

> companies had purchased the other four lots. They exchanged telephone numbers, and Mr. Grewal left to think about the proposal. In a subsequent phone call, Mr. Sangha told Mr. Grewal that Mr. Grewal's $1.6 million contribution to the purchase of Lot 5 would be considered an investment in the Project, that Mr. Sangha would arrange for the paperwork to get ready for subdivision, Mr. Sangha would keep accounting records, Mr. Sangha and his companies would get the lands subdivided and bring fully-serviced lots to market, after which Mr. Grewal would receive a share proportionate to his financial contribution to the Project.

[106] This is an accurate summary of Mr. Grewal's evidence, which I accept to be true.

[107] Mr. Grewal testified that in a discussion a day or so later, Jaswant repeated this description of the proposal and confirmed that he would be responsible for completing the subdivision and selling lots. Mr. Grewal also stated that Jaswant assured him that he would keep accurate records of all expenses and that when the Project was completed there would be an accounting with the profits, after payment of all Project expenses, divided according to proven contributions to the Project.

[108] In these discussions, Jaswant was seeking Mr. Grewal's agreement to provide one half of the money needed to close the purchase of Lot 5. Jaswant told Mr. Grewal that he would provide the other half of the necessary funds. These discussions all occurred a short time before the completion date of June 30, 2011.

[109] On or about June 29, 2011, Panorama assigned a 50% interest in the contract to purchase Lot 5 to Grewal Management.

[110] At that time, Mr. Grewal's understanding was that Lot 5 was to be purchased for cash without obtaining any mortgage financing. However, shortly before the completion, Mr. Grewal learned that Panorama would be financing its half of the purchase through a mortgage from Manjeet Kaur Samra, Aman Mander, Azad Mander, and Ravinder Mander (the "Mander Mortgage"), to be secured against a 100% interest in Lot 5. On closing, title to Lot 5 was transferred to Panorama and Grewal Management, with each company having a 50% registered interest as tenants in common. Grewal Management was named as a mortgagor on the Mander Mortgage.

[111] The purchase of Lot 5 completed on June 30, 2011. On that date Grewal Management advanced $1,687,556.50 and Buckley Hogan provided $428,936.70 to pay part of the purchase price for Lot 5. The balance of the funds required to pay the purchase price came from the deposit and the proceeds of the Mander Mortgage in the principal amount of $1,000,000.

[112] Based on the evidence before me it therefore appears that, with the possible exception of $100,000, Panorama did not provide any of its own funds or any funds provided by Jaswant or other companies he owned for the purchase of Lot 5. Panorama's contribution to the amount necessary to complete the purchase of Lot 5 came from the proceeds of the Mander Mortgage, the deposits from purchasers referred to above, and the initial deposit of $300,000, $200,000 of which came from the funds 0892995 had provided to the October 2010 Joint Venture.

[113] On or about June 30, 2011, Grewal Management and the November 2010 Joint Venturers executed the 2011 JVA.

[114] The 2011 JVA divided Panorama's 28.5% proportionate share in the November 2010 Joint Venture in half, resulting in Panorama's and Grewal Management's respective shares being 14.25%. It also provided that all of the terms of the November 2010 JVA not expressly amended remained in full force and effect.

[115] Counsel has accurately summarized Mr. Grewal's evidence that Jaswant made the following statements to him in June 2011, some of which I have already discussed and some which I will address later in these reasons:

1. Jaswant reassured Mr. Grewal that the same terms in their oral agreement were applicable and Mr. Grewal understood that the registered owners would hold the land in trust;

2. Jaswant did not inform Mr. Grewal about the 2007 JVA or the Garchas' interest in the Project;

3. Jaswant told Mr. Grewal that he had paid the deposit for Lot 5; and

4. Jaswant told Mr. Grewal that Lots 1 to 4 in the Project had been purchased by him and his companies.

[116] I accept that Jaswant made the above statements to Mr. Grewal. I also accept that Jaswant did not inform Mr. Grewal about the Gill Judgment or Ms. Johl's certificate of pending litigation (both discussed below), each registered on certain Project lands.

[117] Mr. Grewal also testified that he had not seen the November 2010 JVA when he signed the 2011 JVA. While I accept his evidence to this effect, I do note that the 2011 JVA makes express reference to the November 2010 JVA and that there is no evidence that Mr. Grewal asked to see that document.

Mr. Mattu's investment

[118] Mr. Mattu invested in the Project before the execution of the November 2010 JVA and before Rajpreet became an investor. In or about 2007, Jaswant requested that Mr. Mattu advance him $400,000 as a loan, in consideration of which Jaswant would pay $500,000 to Mr. Mattu from the profits from Sangha Group 2. Later, Jaswant and Mr. Mattu agreed that rather than paying him $500,000, Jaswant would convert that amount into an investment by Mr. Mattu in the Project. Jaswant acknowledged in cross-examination that he and Mr. Mattu had agreed that the $500,000 would be converted into an investment in the Project, albeit on different terms than alleged by Mr. Mattu.

[119] Mr. Mattu made a number of advances in addition to the $500,000 of Sangha Group 2 proceeds. He testified that, with the exception of some funds advanced to Jaswant for the rebuilding of a house that had been damaged by fire, all of his further advances were made as an investment in the Project. However, Jaswant testified that at a certain point he and Mr. Mattu agreed that Mr. Mattu would become his "silent partner" in all of his real estate investments.

[120] In cross-examination, Jaswant admitted to agreeing with Mr. Mattu that $500,000 of the net proceeds from Sangha Group 2 was to be invested on

Mr. Mattu's behalf in the Project. I accept his evidence on this point, quoted from Mr. Mattu's counsel's argument:

> Q. Mr Sangha, I just want to clarify this: in the responses you just gave, am I correct that what you're testifying is this, when there funds flowing to 690 from the Sangha Group 2 subdivision, $500,000 of that money that came out of Sangha Group 2 subdivision was invested in the 60th Avenue subdivision on behalf of Mr. Mattu?
>
> A. Yes, that's correct.

[121] I am satisfied that the arrangements made with respect to obtaining Mr. Mattu's $500,000 investment and a further $488,791.45 advance on February 15, 2008, materially assisted in the acquisition and carrying costs of the Lots that went into the Project. On a balance of probabilities, given the proximity between the date of the further advance and the dates of June 23 and August 8, 2008, when 690174 advanced $211,490 and $388,227.53 to Buckley Hogan for the purchase of Lots 3 and 4, I find that most of Mr. Mattu's 2008 advance was used to pay the cash due on closing of those Lots. I also conclude that a number of further advances made by Mr. Mattu were used by 690174 or Jaswant to pay interest and other Project expenses.

[122] Jaswant's evidence about when the partnership he alleges with Mr. Mattu was formed is somewhat confusing. He denies that Mr. Mattu was his partner in Sangha Group 1 or 2. The thrust of his evidence appears to be that the partnership came into existence at or about the time that Jaswant became involved in another deal with Hardeep Singh Gill to have 690174 purchase land in Maple Ridge from Mr. Gill.

[123] Mr. Mattu testified that no such agreement was made. Except where I expressly state otherwise, I prefer the evidence of Mr. Mattu when it conflicts with that of Jaswant on this issue.

[124] The Trustee submits that Mr. Mattu admitted he was Jaswant's silent partner to Jaswant's lawyer, Sean Hogan. I accept that Mr. Mattu described himself as a silent partner in a telephone conversation with Mr. Hogan on or about February 21, 2014. This conversation occurred in the context of the preparation of mortgage

documents over the phase 1 lots created by the Project in favour of the 2011 Joint Venturers.

[125] My conclusion, based on the evidence and the inherent unreliability of Jaswant's testimony, is that his testimony that Mr. Mattu was his silent partner in all of his dealings was not true. There is no written partnership agreement between Jaswant and Mr. Mattu. Jaswant did not communicate the existence of any such partnership with Mr. Mattu to anyone prior to this litigation. In particular, Jaswant did not disclose the existence of this partnership to the Trustee or in his statement of affairs in his bankruptcy. If such a partnership existed, it was Jaswant's legal duty to disclose it to the Trustee at the outset of his bankruptcy. He did not.

[126] Mr. Hogan prepared a memorandum of his dealing with respect to the mortgage described in para. 124. In that memorandum he recorded that his assistant had received instructions from Mr. Grewal and Ranjit to add Mr. Mattu as a mortgagee on the mortgage that was being prepared.

[127] Mr. Hogan was called as a witness by the defendants who introduced the memorandum into evidence. In my view the memorandum gives some insight into the nature of Mr. Mattu's involvement in the Project. While Mr. Hogan's assistant was not called as a witness, I am satisfied that the memorandum does accurately record the events leading up to its preparation.

[128] The memorandum states that it was Mr. Grewal and Ranjit Sangha who had first described Mr. Mattu as a silent partner. The context in which this statement was made makes it obvious that they were referring to Mr. Mattu as a silent partner in the Project. It is also apparent that by the time this memorandum was prepared in February 2014, there were financial pressures being put on the Project and that Mr. Mattu was attempting to document and protect his investment.

[129] I am satisfied that when Mr. Mattu referred to himself as Jaswant's silent partner in his phone call with Mr. Hogan he was referring to his investment in the Project and his attempt to be added to the mortgage over the subdivided lots. That conclusion is consistent with the subject matter of the discussion, because it

appears that Mr. Mattu was attempting to obtain the same security for his advances to the Project that the registered members of the 2011 JVA were pursuing.

[130] There is no doubt that Mr. Mattu became heavily involved in the affairs of the Project as time went on. However, in my view, that involvement was consistent with his evidence that he agreed to become involved in the pursuit of the Project and that he had advanced a considerable amount of money to the Project by 2014.

[131] Mr. Mattu's investment was not a loan. There was no evidence that Jaswant or any of his companies assumed any obligation to repay Mr. Mattu's advances, nor was there evidence of any of the usual terms of a loan, such as the rate of interest.

[132] For reasons I will set out later, I have concluded that the agreement made between Mr. Mattu and Jaswant had all of the essential elements of a joint venture agreement pursuant to which Mr. Mattu acquired a beneficial interest in the Project.

[133] There is some dispute between Mr. Mattu and the Trustee over the actual amount Mr. Mattu advanced to the Project. Mr. Mattu submits that the net amount advanced on his behalf, after taking into account funds he received back, was $1,280,350.20. The Trustee's submission is that the net amount of Project-related advances was $894,991.25. The parties are in agreement on the amount of payments back to Mr. Mattu. However, they do not agree that all amounts advanced by Mr. Mattu were advanced for the benefit of the Project.

[134] In 2008, Mr. Mattu raised $488,791 to invest in the Project by mortgaging a property he owned. I agree with the Trustee's submission that the expenses incurred by Mr. Mattu in obtaining that mortgage should not be considered to be an investment in the Project. Mr. Mattu's key allegation is that he invested pursuant to an agreement that the investment would entitle him to an interest in the Project. In my view, the costs associated with raising the funds to be invested should be for Mr. Mattu's account and not treated as a Project investment.

[135] I therefore agree with the Trustee that the following expenses should be deducted from Mr. Mattu's investment:

1.	July 10, 2009: Cunningham and Rivard Appraisal	$870
2.	September 3, 2009: further appraisal fee	$1500
3.	September 9, 2009: Cheque to Hashmi relating to refinancing	$108,000
4.	September 29, 2009: Cunningham and Rivard	$1,938.75

[136] In addition, I agree with the Trustee that the advances on October 25, 2007, of $80,000 and December 5, 2007, of $26,000 have not been shown to relate to the Project and should not be allowed.

[137] I accept Mr. Mattu's evidence that the balance of the amounts he lists were advanced as an investment in the Project. I therefore find that Mr. Mattu's investment, net of repayments, was $1,062,041.45.

[138] On the evidence, it is clear that the funds advanced by Mr. Mattu made a material contribution to the acquisition of Lots 2 to 4 and to the successful completion of the Project.

Rajpreet Sangha's investment

[139] I accept Rajpreet's evidence with respect to his investment in the Project.

[140] In September or October 2010, Mr. Mattu asked Rajpreet if he would be interested in investing in a real estate project. Mr. Mattu knew Rajpreet because he had made deliveries to Rajpreet's convenience store. When Rajpreet expressed interest, Mr. Mattu introduced him to Jaswant.

[141] Jaswant came to Rajpreet's house and told him that he had the right to acquire lots in a subdivision project. Jaswant described the Project and proposed that Rajpreet, Mr. Mattu, and himself each put up $800,000 to acquire 7 lots each from the subdivided lots to be created by the Project. Rajpreet went to view another

project that Jaswant was involved in at 50th Ave. and Number 10 Highway and decided to invest in Jaswant's proposal. Rajpreet asked Jaswant how to do so and Jaswant advised him to set up a company to make the investment. Rajpreet then incorporated 0892995. Jaswant told him that he would arrange for an agreement to be drawn up and would be responsible for taking all necessary steps to complete the proposed agreement.

[142] Jaswant arranged a meeting at Buckley Hogan in October 2010 where the October 2010 JVA was signed by 0892995, 0731431 (Mr. Mattu's company), and Panorama. Rajpreet testified that Mr. Mattu and Jaswant agreed to contribute $800,000 to the October 2010 Joint Venture. This evidence is consistent with the terms of the October 2010 JVA.

[143] The October 2010 JVA stated that it was formed for the purpose of acquiring certain subdivided lots in the Project, building homes on those lots, and selling them. The Preamble to the agreement stated that Panorama had the beneficial right to acquire those lots. Each party agreed to advance a minimum of $800,000 to be used for the purpose of pursuing the objects of the joint venture.

[144] The October 2010 JVA contained terms relevant to the issues in these proceedings, including:

1. In paragraphs 4.1 and 4.2, the October 2010 Joint Venturers agreed that each owned as tenants in common as their separate property an undivided beneficial one-third interest in the in the assets of the October 2010 Joint Venture.

2. Paragraph 9.4 provided that all receipts and disbursements with respect to the October 2010 Joint Venture would be made to a separate bank account maintained solely for that purpose.

[145] A few days after the October 2010 JVA was signed, Jaswant asked Rajpreet for $200,000. On or about October 25, 2010, 0892995 provided Panorama with a bank draft for $200,000. I find that these funds were provided pursuant to the terms of the October 2010 JVA. However, Jaswant did not use them for that purpose. It is

not disputed that all of those funds were instead used as part of the deposit paid for the purchase of Lot 5. I find that Jaswant did not seek or obtain Rajpreet's consent to use the funds for that purpose.

[146] In December 2010, Jaswant told Rajpreet that lots in another project in which he was involved were not selling and that he could not come up with his contribution to the October 2010 Joint Venture. Mr. Mattu said that he would not contribute his $800,000 if Jaswant did not provide his funds. However, Jaswant said he had a new proposal for Rajpreet. He proposed that instead of investing in the October 2010 Joint Venture, Rajpreet should invest in the Project.

[147] Jaswant's proposal was that the funds that 0892995 has already provided, together with an additional $600,000, would be invested in the Project and that the profits from the Project would be divided in accordance with the contributions of each investor. Rajpreet agreed to proceed on that basis, providing Panorama with a bank draft for $300,000 and sometime later with $300,000 in cash.

[148] I find that Rajpreet provided these funds as an investment in the Project. I also infer that it was understood that the funds would be invested on the same terms as the October 2010 JVA; that is, that Rajpreet's investment would entitle him to a beneficial ownership interest in the Project based on his contribution.

[149] On November 17, 2010, Panorama paid a deposit of $300,000 on account of the purchase price for Lot 5. It is clear that $200,000 of that amount came from funds advanced by 0892995 pursuant to the October 2010 JVA.

[150] Schedule 6 of Exhibit 175, the Trustee's Summaries, indicates that $50,000 was transferred from Best Quality Homes Ltd. to Panorama on May 2, 2011, and that $10,000 was transferred on April 14, 2011. The Trustee attributes these transfers to funds provided by Rajpreet. Thus, even using the first in, first out ("FIFO") method of accounting used by the Trustee, which for reasons I will set out below I do not agree with, some $260,000 of funds provided by Rajpreet have been shown to have been used to acquire Lot 5.

[151] Jaswant may have used some of the funds advanced by 0892995 for purposes other than the Project. The evidence before me does not disclose what exactly Panorama used those funds for. However, I infer that most of the funds he provided were used to finance expenses related to the Project.

[152] By the time that Rajpreet made his last advance of $300,000, the November 2010 JVA had been executed. Therefore, the only means by which he could participate in the Project was by acquiring an interest in the November 2010 Joint Venture.

[153] I accept Rajpreet's evidence that he was not aware of the terms of the November 2010 JVA. However, I find that he had a reasonable expectation, based on Jaswant's proposal, that he would participate in the Project through having a proprietary interest in its assets.

[154] Jaswant admits to receiving $800,000 from Rajpreet and 0892995 but denies that he agreed that the advances were an investment in the Project. However, Jaswant was unable to give any other explanation as to the basis on which he obtained Rajpreet's funds.

[155] I am satisfied on the evidence that Jaswant was in need of funds to acquire Lot 5 when he made the agreements with Rajpreet and obtained his investment. I am also satisfied that a substantial portion of the funds advanced by Rajpreet made a direct contribution that was vital to the success of the Project, including paying the deposit for the purchase of Lot 5 and a substantial portion of the development costs for that Lot.

[156] By the time the November 2010 JVA was executed, 690174 had already acknowledged that it held title to Lot 1 as bare trustee for the participants in the October 2007 JVA. In addition, Panorama had also agreed that it would hold title to certain lots that it would receive from the subdivision of the 5 Lots as bare trustee for the participants in the October 2010 JVA. Jaswant and Mr. Mattu had also made the agreement whereby Mr. Mattu had invested more than $1,000,000 in the Project.

[157] Notwithstanding these previous agreements, in the November 2010 JVA 690174 covenanted that it was the beneficial owner of Lot 1 and Panorama covenanted that it had the right to become the beneficial owner of Lot 5. On the evidence before me the covenant with respect to Lot 1 was demonstrably untrue and the covenant with respect to Lot 5 was misleading because Panorama lacked the funds necessary to purchase Lot 5.

[158] In the result, by June 30, 2011, Jaswant and his companies had entered into a number of agreements with respect to the Project that conflicted with each other. This litigation arises as a direct consequence of those actions.

The Gill Judgment and Johl claim against 690174

[159] The Gill Judgment and the Johl Certificate of Pending Litigation are of fundamental importance to these proceedings. I will therefore describe them in some detail.

[160] 690714 appears to have been Jaswant's main operating company before he became involved in the Project. Notwithstanding the fact that 690174 agreed to hold legal title to Lot 1 in trust for the October 2007 Joint Venturers, Jaswant continued to carry on business unrelated to the Lot 1 Project in that company. He also failed to take any steps to insulate Lot 1 from 690174's other business activities, such as, for example, transferring the legal title to Lot 1 to another single-purpose legal entity.

[161] On or about November 19, 2007, one month after the 2007 JVA was executed, Jaswant caused 690174 to enter into an agreement with Hardeep Singh Gill to purchase property from him for development purposes. For reasons that were not put into evidence, 690174 did not complete its contract to purchase that property. As a result, Mr. Gill commenced an action against 690174 in this Court on May 12, 2009, alleging that 690174 had breached its contract to purchase the property and seeking specific performance or damages in lieu thereof for the breach.

[162] 690174 filed a statement of defence in the action on June 9, 2009, but on November 27, 2009, Mr. Gill obtained a judgment against it in the amount of approximately $750,000, plus costs.

[163] On December 1, 2009, Mr. Gill registered the Gill Judgment against Lot 1 in the Land Title Office. I find that Jaswant was fully aware of this action and of the 2009 registration of the judgment. Pursuant to s. 89(2) of the *Court Order Enforcement Act,* R.S.B.C. 1996, c. 78, the Registrar of Land Titles must send a notice of the registration of a certificate of judgment together with a copy of the certificate of judgment to the registered owner of the property against which it has been registered. I therefore infer that Jaswant was aware of the registration of the Gill Judgment in January 2010, when he had the 2007 Joint Venturers execute the amendment to the 2007 JVA. I find that Jaswant did not inform the other 2007 Joint Venturers of the registration of the Gill Judgment at that time or thereafter.

[164] On October 14, 2010, Sarabpaul Kaur Johl commenced an action against 690174 and Jaswant seeking an order for specific performance or damages in lieu thereof in respect of an agreement she alleged she had made to purchase a lot that was to be subdivided from Lots 1 and 2 of the Project. Pursuant to this action, Ms. Johl filed a Certificate of Pending Litigation against Lots 1 and 2 in the Land Title Office on October 27, 2010 (the “Johl CPL”). I note that this was very close in time to the October 2010 JVA.

[165] It is common ground that the registration of the Gill Judgment and the filing of the Johl CPL prevented the registration of any subdivision plan as long as they remained registered. It is also clear that no institutional financing could have been obtained on the security of lands registered in the name of 690174 or the registered owners of Lot 2 as long as these charges remained on title to the Project lands.

[166] I find that Jaswant did not disclose the Gill Judgment or the Johl CPL to the Garchas, Mr. Grewal, or Rajpreet prior to June 2011. However, it is probable that Mr. Mattu was aware of them because of his involvement in the Project.

The Virk Mortgage

[167] Despite the registration of the Gill Judgment and the Johl CPL, Jaswant continued with efforts to complete the subdivision of Lots 1 to 5. However, it was critical that these charges be removed from title before the subdivision could be

completed. To that end, in the fall of 2011 Jaswant arranged a loan from Jatinder Virk, Mr. Grewal's sister-in-law, in the amount of $900,000 to provide security for the discharge of the Gill Judgment and Johl CPL.

[168] A number of complex steps were taken to provide security for the loan from Ms. Virk without the registration of a mortgage against Lots 1 to 5. The loan was structured as a loan to Mr. Mattu, his wife, and Raveen, secured by a mortgage over two properties owned by the Mattus and the property registered in Raveen's name on which Jaswant and Parmjit resided. Mr. Mattu and his wife were named as co-borrowers on this mortgage. This mortgage was registered in the New Westminster Land Title Office on October 14, 2011.

[169] As further security for her loan, Ms. Virk was granted two unregistered mortgages over a number of properties, including Lot 1, Lot 3, the undivided half interest in Lot 5 registered in Panorama's name, Jaswant's interest in Lot 4, and Jaswant and Parmjit's interest in Lot 2.

[170] The unregistered mortgages were executed on October 13, 2011, and were held in escrow by a law firm in Surrey subject to conditions for release to the mortgagee on certain events of default.

[171] The proceeds of the Virk mortgage were used to provide security to discharge the Gill Judgment and the Johl CPL from title to the affected properties, thus permitting the Project to move forward. However, the success of the Project thereby depended on its completion and sale before the Virk mortgage became enforceable. In addition, the Virk Mortgage added over $1,000,000 in debt secured by some of the Project lands, including Lot 1.

[172] In these proceedings Jaswant has acknowledged that the Virk Mortgage was his responsibility because it was taken out to satisfy an obligation that was unrelated to the Project and for his sole benefit.

[173] I take Jaswant's statements to be an acknowledgement that he was using Lot 1 for an improper purpose. I find that he was aware of the impropriety of his actions at the time he undertook them.

[174] The arrangements made with Ms. Virk did however permit mortgage financing to be obtained and allowed the subdivision to proceed.

The Ludu Mortgage

[175] On December 9, 2011, Jaswant and Parmjit granted a mortgage of Lot 3 to Rattan Singh Ludu, securing the principal amount of $270,250 with an annual interest rate of 25% (the “Ludu Mortgage”).

[176] The Ludu Mortgage was granted after the execution of the joint venture agreements and, in particular, after Jaswant and Parmjit had agreed that their legal title to Lot 3 was held beneficially for all of the members of the 2011 Joint Venture.

[177] The proceeds of the Ludu Mortgage were paid to Jaswant and Parmjit. There is no evidence that the proceeds of the Ludu Mortgage were used in the Project. In his Preliminary Report, the Trustee stated that little is known about this mortgage. However, in the Agreed Statement of Facts the parties agreed that on December 12, 2011, the solicitors who acted on behalf of the mortgagee issued a cheque for $250,000 to Jaswant and Parmjit. I find that this cheque was the net amount advanced under the Ludu Mortgage and that Jaswant and Parmjit have not shown that these funds were used in the Project.

The WSCU mortgages

[178] On February 10, 2012, Westminster Savings Credit Union (“WSCU”) issued a commitment letter to 690174 and the other 2011 Joint Venturers granting approval of development financing to complete the Project. Mr. Grewal and his wife Gurmeet Grewal (the “Grewal Guarantors”) agreed to guarantee the WSCU financing. The commitment letter provided for a first advance to discharge all Acquisition Mortgages. It also provided for subsequent advances pursuant to a development mortgage.

[179] On March 19, 2012, WSCU advanced the sum of $6,603,604.65 pursuant to its mortgage. This advance paid out the outstanding balances on all of the Acquisition Mortgages.

[180] The following table sets out the amount advanced under each of the Acquisition Mortgages and the amounts advanced to pay out the outstanding balances owing, as set out in the Agreed Statement of Facts:

Acquisition Mortgage or Replacement	**Original Balance**	**Paid March 2012 (to nearest dollar)**
1. PCMIC Mortgage Lot 1	$1,750,000	$1,948,596
2. TD Canada Lot 2	$750,000	$668,951
3. RBC Lot 3	$945,000	$845,029
4. G&F Credit Union Lot 4	$994,196	$927,041
5. Mander Mortgage Lot 5	$1,000,000	$1,115,974

[181] In addition, $740,498 was paid to Grewal Management, $322,206 was used to repay the Ludu Mortgage, and $34,905 was paid to the City of Surrey for taxes from the proceeds of the WSCU Mortgage.

[182] On June 13, 2012, the 2011 Joint Venturers executed a further mortgage in favour of WSCU to provide construction financing of up to $6,082,500 for the Project. In connection with this mortgage, the 2011 Joint Venturers also executed a construction loan agreement setting out the terms on which funds would be advanced. As part of the financing arrangements with WSCU, a Project chequing account was established at WSCU. Cheques drawn on this account required the signatures of any two of Jaswant, Ranjit, and Mr. Grewal. While it is not expressly set out in the evidence, it appears that Project expenses from that date forward were paid from this account.

The Land Swap Agreement and subdivision

[183] As part of the Project, Jaswant negotiated a land swap agreement (the “Land Swap Agreement”) with the Anglican Diocese of New Westminster, whereby a portion of Lot 1 was exchanged for a portion of a large lot owned by the Diocese

adjacent to Lot 1. This swap increased the number of subdivided lots that could be created from the Project.

[184] The Land Swap Agreement was dated June 1, 2011, but was actually executed on or about January 3, 2012. It contemplated 690174 acting as a developer and registering certain subdivision plans to give effect to the agreement. As part of that process the 2011 Joint Venturers and the Synod of the Diocese of New Westminster conveyed their interests in the Project lands and the Diocese lands to Raveen in trust for purposes of subdivision.

[185] On November 29, 2012, Raveen consolidated and subdivided Lots 1 to 5 and the Diocese Lands into 30 lots, one of which was conveyed to the Diocese (the "Church Lot").

Subdivision of Lots

[186] After the Land Swap Agreement was completed and the Church Lot was conveyed to the Diocese of New Westminster, two further subdivisions were effected, resulting in the creation of 81 subdivided lots in total.

[187] The steps taken to effect the subdivisions are set out in paragraphs 120 to 136 of the Agreed Statement of Facts and I need not repeat them here. The registered titles to the subdivided lots varied from the proportionate ownership interests of the parties set out in the 2011 JVA. However, the 2011 JVA provided that the registered interest in each lot was held by the registered owner or owners of that lot in trust for all of the members of the 2011 Joint Venture in accordance with their proportionate shares set out in that agreement.

[188] Beginning in 2010, although there was no evidence before me to indicate that proper regulatory approval had been obtained to do so, Jaswant began entering into agreements to sell lots in the Project. Once the subdivision plans had been registered, lot sales began to be completed. The first receipts for these lots were paid to WSCU to pay down the amount secured by its mortgages.

Further legal proceedings

[189] On March 14, 2014, Jatinder Virk commenced foreclosure proceedings against Lot 3. On September 2, 2014, she amended her petition to seek a declaration of a prior mortgage affecting the lots created by the Project and filed a certificate of pending litigation against those lots in the New Westminster Land Title Office. These steps temporarily prevented completion of the sale of further lots in the Project.

[190] The Grewal Action was commenced on April 2, 2014. In general terms, it alleged that the Grewal plaintiffs had the right to share in the proceeds of sale of the subdivided lots based on contributions to the Project made pursuant to oral agreements with Jaswant, 690174, and Panorama.

[191] On or about July 17, 2014, Jaswant provided a demand promissory note from 690174 payable to Mr. Garcha as lender in the amount of $484,252 (the “Promissory Note”). The Promissory Note stated that the lender agreed that this amount represented the amount paid to 690174 as the lender’s contribution to the 2007 Joint Venture. However, the note was not signed by Mr. Garcha.

[192] On October 7, 2014, WSCU began foreclosure proceedings to enforce its mortgage security over the subdivided lots and filed certificates of pending litigation in respect of its mortgage against all of the subdivided lots.

[193] The Garcha Action was commenced on February 16, 2015, asserting that the Garchas had rights pursuant to the 2007 JVA. In it, Mr. Garcha also sought judgment on the Promissory Note.

[194] 690174 did not defend the Garcha Action, and on March 17, 2015, Mr. Garcha took default judgment on the Promissory Note in its amount together with costs and Court Order Interest.

[195] On May 19, 2015, Justice Harvey granted an order *nisi* of foreclosure in the Jatinder Virk foreclosure proceedings (the “Harvey Order”). The Trustee places considerable reliance on this order, because in it the Court declared that the Virk

mortgage ranked in priority to the interests of the respondents and those claiming by, through, or under them. The Garchas were named as respondents in this foreclosure proceeding, although it appears that their counsel did not attend at the hearing.

[196] One week later, on May 26, 2015, Justice Masuhara made an order in petition S-153116, commenced by other members of the 2007 Joint Venture, converting that petition to an action and setting out a sales procedure for the remaining unsold subdivided lots. This order expressly reserved the rights of all parties.

[197] On August 24, 2015, Jaswant made a voluntary assignment in bankruptcy, and Crowe Mackay & Company was appointed as his Trustee.

[198] On April 18, 2016, the Trustee obtained leave of the Court to assign 690174 and Panorama into bankruptcy. Those companies were assigned into bankruptcy on April 21, 2016, with Crowe Mackay being appointed Trustee in both bankruptcies.

[199] On May 11, 2016, the Court made a sales process order in these proceedings which resulted in all proceeds from the sale of lots, after payment of the WSCU Mortgage, being placed in trust with the Trustee's counsel for the 2011 Joint Venturers. The proceeds were placed in separate trust accounts depending upon which 2011 Joint Venturer was the registered owner of the lot from which the proceeds were derived (the "Vendor Trust Accounts"). However, the Trustee recognizes that the amounts attributed to each party must be adjusted to reflect their proportionate interests set out in the 2011 JVA.

[200] By October 28, 2016, all lots had been sold and the net proceeds deposited with the Trustee's solicitors in the Vendor Trust Accounts.

[201] The net proceeds of sale after satisfaction of the amounts owed to WSCU were $15,441,090.52. From those proceeds, $1,602,942.51 was paid to satisfy the Virk Mortgage. In addition, builders liens of $410,734.62 and $37,110.34 were paid from the funds held in trust.

[202] In the course of the administration of the Bankruptcies, the plaintiffs in the Grewal and Garcha Actions filed proofs of claim against the Bankrupts. I need not detail them because, as I have already decided, the rights of the parties will be decided *de novo* in these reasons. It is sufficient to say that the Trustee either disallowed the claims or decided that they were equity claims that were postponed to the claims of all other creditors pursuant to s. 140.1 of the *BIA.*

Issues Raised in the Proceedings

[203] I outlined the orders that have led to this trial in the course of dealing with the procedural issues earlier in these reasons.

[204] The parties raise a multitude of issues. However, in my view, many of the arguments and submissions seek the same result by relying on different theories of liability or defence.

[205] The cornerstone of the Trustee's position is that the claims of the Garcha and Grewal plaintiffs' claims are equity claims, as that term is defined in the *BIA,* and are therefore postponed to the claims of other creditors of the Bankrupts. However, in order to determine that issue I must first consider the nature of the relationships between the plaintiffs and the defendants as well as the nature of the plaintiffs' interests in the Project. I will therefore first determine the rights of the parties without reference to the *BIA*, then consider how the Bankruptcies have affected those rights.

Issues in the Garcha Action

[206] The following issues arise in the Garcha Action:

1. What was the nature of the relationship between the Garchas and 690174 created by the 2007 JVA? Was it a binding agreement and did it create a trust?

2. Did Jaswant and 690174 owe fiduciary duties to the Garchas, and if so, what was the extent of those duties?

3. Did 690174 and Jaswant breach any fiduciary duties they owed to the Garchas?

4. If Jaswant and 690174 breached their fiduciary duties to the Garchas, are any of the other defendants liable to the Garchas on the basis of knowing assistance or knowing receipt?

5. Are the Garchas entitled to a remedy against the lots created by the Project?

6. By taking judgment on the Promissory Note did Mr. Garcha elect a remedy that precludes the Garchas from pursuing their claims to an interest in the subdivided lots?

7. Are any defences raised by the defendants a bar to the remedies sought by the Garchas?

Issues in the Grewal Action

[207] I will deal with the claim of Rajpreet Sangha as part of the Grewal Action even though he represented himself at trial.

[208] The issues raised in the Grewal Action are:

1. What was the nature of the various Grewal plaintiffs' involvement in the Project? In particular, were any binding oral joint venture agreements made between any of the Grewal plaintiffs and the defendants? If there were any such agreements, what were their terms?

2. What is the relevance of the October 2010 JVA?

3. Are the November 2010 and 2011 JVAs valid and binding agreements in accordance with their terms, and if so, what is the relationship between them and the oral agreements alleged by the Grewal plaintiffs? To what extent are the defendants other than Jaswant, 690174, and Panorama bound by those alleged oral agreements?

4. Did Jaswant have the authority to bind the members of the November 2010 Joint Venture to any agreements made with Grewal Management, Mr. Mattu, and Rajpreet?

5. If the alleged oral agreements are established, what remedies are appropriate?

6. Did the Bankrupts owe fiduciary duties to the Grewal plaintiffs, and if so, did they breach those duties? What remedies are appropriate?

7. Do any of the Grewal plaintiffs have a claim in unjust enrichment against the defendants?

Issues in the Bankruptcy Appeals

[209] The following issues arise in the Bankruptcy Appeals:

1. Are the remedies sought by the Garcha plaintiffs and Grewal plaintiffs against the Bankrupts equity claims subordinated to the claims of all other creditors pursuant to s. 140.1 of the *BIA*?

2. What effect do the Bankruptcies have on remedies that might otherwise have been available to the plaintiffs and, in particular, on the granting of constructive trusts over the proceeds of sale of the Project?

Discussion of Garcha Claims

Did the 2007 JVA create a trust of which the Garchas were beneficiaries?

[210] The Garchas' claim is based on their status as signatories to the 2007 JVA. I set out some of the terms of that agreement earlier in these reasons at para. 76.

[211] The Garchas' position is that 690174 and Jaswant owed fiduciary duties pursuant to the 2007 JVA that prevented them from taking any benefit from 691074's legal title to Lot 1, other than 690174's contingent right to the revenue received if Lot 1 was subdivided into more than 22 lots. The Garchas submit that the 2007 JVA

created a trust of which they and the other 2007 Joint Venturers were the beneficiaries that can be traced into the subdivided lots and revenue they generated.

[212] In his evidence, Mr. Garcha testified that his understanding of the 2007 JVA was that in consideration of contributing between $50,000 and $60,000 per lot, he and his wife would receive seven lots once the subdivision of Lot 1 was completed. He testified that Jaswant had described the investment to him this way, and that this was his expectation when he contributed funds to the Project.

[213] Although they initially took a different position, in their final arguments the defendants and the Grewal parties conceded that the 2007 JVA is a valid and binding agreement. However, their position is that it does not create a beneficial interest for the 2007 Joint Ventures in the subdivided lots created by the Project. They say that the elements necessary to create an enforceable trust with respect to those lots are absent in this case.

[214] The Trustee and the Grewal plaintiffs concede that 690174 acquired and held Lot 1 in trust for the 2007 Joint Venturers. However, the Trustee, supported by all of the defendants, takes the position that that trust was extinguished by the development process and that the 2007 Joint Venturers have only a contractual right against 690174 to share in its profits from the Project.

[215] In addition, the defendants submit that if there was an agreement that the Garchas were entitled to receive specific lots created from the subdivision of Lot 1, that agreement did not create a valid trust because it lacked the three certainties required to establish a trust: (i) certainty of intention, (ii) certainty of object, and (iii) certainty of subject matter.

[216] While the Grewal parties do not oppose the Garchas sharing in the proceeds of the Project, they support the defendants' position that the 2007 JVA did not create a valid trust in the subdivided lots because there was no certainty as to the subject matter of the trust. They submit that certainty was lacking because the agreement did not specify which lots each 2007 Joint Venturer would receive on subdivision and provided no mechanism pursuant to which the court could determine that issue.

[217] I do not accept this submission. I find that the subject matter of the trust was Lot 1 and all other assets of the 2007 Venture. I am also of the view that the 2007 JVA adequately describes the rights of the members of the joint venture on the subdivision of Lot 1. It provides a formula for division of the net proceeds of the subdivision, based on the number of subdivided lots created by the subdivision process. In my view the existence of such a formula meets the requirement for certainty of subject matter. In Donovan W.M. Waters et al., *Waters' Law of Trusts in Canada*, 4th ed. (Toronto: Thomson Reuters Canada Limited, 2012) at 163, the principle is stated as follows:

> When the courts say there must be certainty of subject-matter, they mean that the property must either be described in the trust instrument, or there must be a "formula or method given for identifying it". This latter form of certainty more often occurs with fixing the quantum of beneficiaries' interests, but it can occur with the whole trust property.

[218] I agree that the 2007 JVA did not give the Garchas the right to take title to specific lots created by the subdivision. It may be that Mr. Garcha's subjective understanding of the transaction was that he and Ms. Garcha would receive title to seven lots on subdivision, subject to payment of costs of $50,000 to $60,000 per lot. However, subject to certain exceptions that are not present in this case, his subjective understanding is not admissible to vary or alter the express terms of the 2007 JVA.

[219] The Trustee submits that the object and purpose of the 2007 JVA was the subdivision of Lot 1 into residential lots, the sale of those lots, and the division of the net profits after expenses among the 2007 Joint Venturers. His position is that the 2007 JVA is a commercial agreement that limits the rights of the 2007 Joint Venturers to a contractual right to a share of the net profits from the sale of subdivided lots. The Trustee also argues that the commercial nature of the 2007 JVA negates any fiduciary obligations except those that arose out of the bare trust over Lot 1.

[220] The Trustee made extensive written submissions on the principles of contractual interpretation in support of his argument that 690174 owed no fiduciary

duties and that the members of the 2007 Joint Venture had no proprietary interest in the proceeds of sale of lots subdivided out of Lot 1.

[221] I find these submissions to be without merit.

[222] The principles of contractual interpretation are well settled. They were restated by Justice Rothstein in *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53 [*Sattva*] at para. 47:

> Regarding the first development, the interpretation of contracts has evolved towards a practical, common-sense approach not dominated by technical rules of construction. The overriding concern is to determine "the intent of the parties and the scope of their understanding" (*Jesuit Fathers of Upper Canada v. Guardian Insurance Co. of Canada*, 2006 SCC 21, [2006] 1 S.C.R. 744, at para. 27, per LeBel J.; see also *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4, [2010] 1 S.C.R. 69, at paras. 64-65, per Cromwell J.). To do so, a decision-maker must read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract. Consideration of the surrounding circumstances recognizes that ascertaining contractual intention can be difficult when looking at words on their own, because words alone do not have an immutable or absolute meaning:
>
> > No contracts are made in a vacuum: there is always a setting in which they have to be placed... . In a commercial contract it is certainly right that the court should know the commercial purpose of the contract and this in turn presupposes knowledge of the genesis of the transaction, the background, the context, the market in which the parties are operating.
> >
> > (*Reardon Smith Line*, at p. 574, per Lord Wilberforce)

[223] As a general rule the subjective intention or understanding of a party to a contract is irrelevant to its proper interpretation. The object of the interpretation of a contract is to determine what the parties using the words in the relevant circumstances would reasonably have been understood to mean.

[224] I find that the only reasonable interpretation of the 2007 JVA is that each 2007 Joint Venturer is the beneficial owner of their proportionate share of all of the assets of the 2007 Joint Venture. This is made clear by paragraph 4.2, which I have set out above, but will repeat here:

> The Joint Venturers each own as tenants in-common, as their separate property, an undivided beneficial interest in the Project and the Joint Venture Assets in the ratio of their respective Proportionate Shares.

[225] Any doubt about the meaning of this provision is removed by the definition of Joint Venture Assets found at paragraph 1.1(d):

> "Joint Venture Assets" means all property and assets of the Joint Venture, both real and personal, tangible and intangible, including, without limitation, goodwill, interests in contracts, money and bank accounts"

[226] Preambles B and C of the 2007 JVA provide:

> B. The parties have agreed to form a joint venture (the Joint Venture) for the purpose of investing in the Lands for the purpose of developing, subdividing same into approximately 22 RF-9 residential lots and the reselling of the aforesaid lots;
>
> C. The Company (690174) shall hold legal title to the Lands and develop it as bare trustee on behalf of the Joint Venturers;

[227] Paragraph 3.2 of the agreement gives effect to this intention:

> The Joint Venturers hereby associate themselves into and as a joint venture for the purpose of:
>
> a) combining their skills, experience and resources to develop and subdivide the Lands into approximately 22 RF-9 residential lots and resell the aforesaid lots;
>
> b) doing all things incidental thereto;
>
> (together, the "Project")

[228] These provisions clearly spell out that each of the 2007 Joint Venturers is the beneficial owner of an undivided proportionate interest in the assets of the 2007 Joint Venture. At the time the 2007 JVA was executed, title to Lot 1 had already been acquired, utilizing in large part funds contributed by the 2007 Joint Venturers other than 690174. The express purpose of the 2007 Joint Venture was to develop that lot on behalf of all of the 2007 Joint Venturers. From the outset, each of the 2007 Joint Venturers was a beneficial owner of a proportionate share of all of the assets of the 2007 Joint Venture, including Lot 1.

[229] In his written submissions, the Trustee also takes the position that the purpose of the bare trust was "spent" and came to an end upon the subdivision of

Lot 1. In this regard he repeats his submission that as of that date the sole right of the 2007 Joint Venturers was a contractual right to share in the net proceeds after payment of expenses. The Trustee further submits that 690174 had the right and authority to convey legal and equitable title to the subdivided lots to purchasers of those lots, subject only to the contractual obligation to share the profits with the other 2007 Joint Venturers.

[230] These submissions are unsupportable in view of the express terms of the 2007 JVA and the law relating to fiduciary duties that arise in the context of a joint venture.

[231] The rights and obligations arising under a joint venture agreement are of fundamental importance in determining the position of the parties both before and after bankruptcy. The characteristics of a joint venture were addressed by Justice Goldie of the British Columbia Court of Appeal in *Canlan Investment Corp. v. Gettling*, [1997] B.C.J. No. 1647:

> 30 Counsel reviewed for us many authorities on the subject of joint ventures. The chambers judge laid some emphasis on the fact that from the outset it was intended the two venturers would own shares in a company owning and operating the ice facility, rather than having a direct property interest in that facility. Thus, the relationship of the two would be governed not by a joint venture agreement but by company law applied to a shareholders' agreement. He was influenced by the judgment of the *Nova Scotia Supreme Court in Central Mortgage & Housing Corp. v. Graham* (1973), 43 D.L.R. (3d) 686 where Mr. Justice Jones canvassed the existing authorities with particular reference to *Williston on Contracts*, 3d Ed., (N.Y.,1959).
>
> 31 I refer, as did Mr. Justice Jones, to pp. 563-5 of this text, and in particular to p.563:
>
> > Besides the requirement that a joint venture must have a contractual basis, the courts have laid down certain additional requisites deemed essential for the existence of a joint venture. Although its existence depends on the facts and circumstances of each particular case, and while no definite rules have been promulgated which will apply generally to all situations, the decisions are in substantial agreement that the following factors must be present:
> >
> > (a) A contribution by the parties of money, property, effort, knowledge, skill or other asset to a common undertaking;
> >
> > (b) A joint property interest in the subject matter of the venture;
> >
> > (c) A right of mutual control or management of the enterprise;

> (d) Expectation of profit, or the presence of "adventure," as it is sometimes called;
>
> (e) A right to participate in the profits;
>
> (f) Most usually, limitation of the objective to a single undertaking or ad hoc enterprise.
>
> [Emphasis added by Justice Goldie]
>
> 32 While the "decisions" referred to are mainly from jurisdictions in the United States, I regard the foregoing when read with the 1993 supplement as a reasonable and compendious statement of the characteristics of a joint venture.

[232] *Canlan* was cited by Justice Wedge in *Blue Line Hockey Acquisition Co., Inc. v. Orca Bay Hockey Limited Partnership*, 2008 BCSC 27, which has in turn been cited in a number of subsequent decisions of this Court.

[233] The above quotation recognizes that the members of a joint venture have a joint property interest in the subject matter of the joint venture. Unlike a partnership, a joint venture does not own the property that is the subject matter of the joint venture. Instead, the persons forming the joint venture own the property in their proportionate shares, unless the parties make an agreement to the contrary.

[234] The rights, including the property rights, of the 2007 Joint Venturers must be determined by the terms of the 2007 JVA. In my view those terms make it clear that each 2007 Joint Venturer is the beneficial owner of its proportionate share of the assets of the 2007 Joint Venture. It is that beneficial ownership that entitles them to share in the net proceeds of the 2007 Joint Venture. This right is not derived through 690174, as the Trustee seems to have assumed.

[235] The nature of the ownership of property that is the subject matter of a joint venture was considered by the Alberta Law Reform Institute's 2012 publication *Joint Ventures, Final Report 99* at page 18:

> If joint ventures are allowed to declare themselves not to be partnerships, questions may arise as to ownership of property owned by the non-partnership joint venturers respectively and committed to the joint venture, and as to the ownership of property acquired in the course of the joint venture. If the joint venture contract provides for the ownership of the property, its provisions will prevail. If the joint venture contract is silent on the question, in the absence of any legislative provision, property committed by a joint venturer for the use of the joint venture will presumably remain the

> property of the joint venturer, while property acquired in the course of the joint venture will presumably be co-owned by the joint venturers.

[236] I also conclude that the beneficial ownership interests of the 2007 Joint Venturers are traceable into 690174's proportionate share of the 2011 Joint Venture and do not form part of the assets of 690174 divisible among its creditors.

690174 and Jaswant owed fiduciary duties to the 2007 Joint Venturers

[237] I find that 690174 and Jaswant owed a fiduciary duty to the 2007 Joint Venturers by virtue of the terms of the 2007 JVA and Jaswant's *de facto* control of its affairs.

[238] The preponderance of authority establishes that the members of a joint venture owe fiduciary duties to the joint venture and to one another when they are dealing with the property or enterprise that is the subject of the joint venture. Those duties are restricted to the objects of the joint venture and may be altered by agreement or by the particular circumstances of a case. In this regard, the members of a joint venture are not generally restricted from carrying on other activities that they might be precluded from pursuing if they were in a partnership.

[239] I adopt the analysis of the circumstances in which fiduciary duties in a joint venture arise set out by Justice Butler, when he was a member of this court, in *Smithies Holdings Inc. v. RCV Holdings Ltd.*, 2014 BCSC 1688. In my view, the following paragraphs from *Smithies Holdings* apply to the duties owed by 690174 pursuant to the 2007 JVA:

> 73 The finding that a disclosure obligation may arise by implication from the terms of the JV Agreement does not preclude a finding that the Joint Venturers are in a fiduciary relationship. The fact the obligation arises between them in relation to the management of the JV is important. Messrs. Hong, Smithies and Vandekerkhove, as officers and directors of Spearpoint, were placed in the position of fiduciaries with regard to the management of that company. Of course, the management tasks of the company are restricted to the business of the JV. The Lands, the primary asset of the JV, are held in trust by Spearpoint, and pursuant to Article 6 of the JV Agreement, the Board of Directors of Spearpoint is responsible for the "overall management and control of the Joint Venture". Given this structure, it is difficult to see how the obligation of honesty and good faith owed by the individuals as directors and officers of Spearpoint, does not also apply to the Joint Venturers in relation to their dealings with the business of the JV. Of

> course, as directors and officers of Spearpoint the individuals are in a per se fiduciary relationship with one another. As Joint Venturers, they cannot escape the nature of that relationship just because the business of Spearpoint is one step removed from the JV.
>
> 74 In addition, it is difficult to see how the terms of the JV Agreement which permit the Joint Venturers to compete in other land transactions could eliminate the existence of the obligation of full disclosure in relation to this common venture. In other words, while the nature of the obligations owed may be reduced or narrowed by the terms of the JV Agreement, the Joint Venturers remain in a common venture and there is no principled reason why they should not continue to owe the duties of full disclosure and a duty not to make a secret profit in relation to this common venture. I conclude the parties were in a per se fiduciary relationship.

[240] In *Zynik Capital Corp. v. Faris*, 2007 BCSC 527, Justice Tysoe emphasized that fiduciary duties are not owed between parties who are negotiating for a joint venture but do arise after they have entered into one:

> 131 Counsel for Mr. Faris (whose submission in this regard was adopted by counsel for Intergulf) submits that no concurrent fiduciary duties were owed because Intergulf and Zynik were sophisticated commercial entities dealing at arm's length with no power imbalance between them. In my view, a distinction must be made between negotiations for the creation of a joint venture and dealings after the joint venture has been formed. I accept that parties who are negotiating with each other at arm's length to form a joint venture will not owe fiduciary duties to each other. However, the situation changes once the joint venture is formed. For example, in the context of this case, I think it is clear that, during the subsistence of the joint venture, both Zynik and Intergulf owed each other the fiduciary duty not to acquire the opportunity for themself to the exclusion of the other.

[241] In this case 690174 held title to Lot 1 in trust for the 2007 Joint Venturers. 690174 agreed that as bare trustee of Lot 1 it was responsible for applying for all necessary permits required for the development and subdivision of Lot 1. The development and subdivision of Lot 1 was the very object of the 2007 Joint Venture. In addition, Jaswant was personally appointed manager of the 2007 Joint Venture project and was the sole director and directing mind of 690174. In my view this gave rise to a *per se* fiduciary duty on 690174 and Jaswant.

[242] I am also satisfied that the circumstances of this case imposed an *ad hoc* fiduciary duty on 690174 and Jaswant. Given the terms of the 2007 JVA and the fact that it was clear that Jaswant assumed full control over the affairs of the 2007 Joint Venture, I find that the 2007 Joint Venturers had the right to expect that 690174

and Jaswant would act in the mutual interests of the parties to the 2007 JVA to the exclusion of their several interests: *Hodgkinson v. Simms*, [1994] 3 S.C.R. 377 at 407.

[243] The Trustee relied on the fact that 690174 was a bare trustee of Lot 1 and cited a number of cases in support of the proposition that a bare trustee owes only a limited fiduciary duty to the beneficiaries of the trust. However, those cases do not stand for the proposition that the bare trustee may treat the subject matter of the trust as its own property. As pointed out in one of the Trustee's authorities, *Scoretz v. Kensam Enterprises Inc.*, 2018 BCCA 66 at paras. 21-30, at a minimum a bare trustee has the obligation to transfer legal title to the beneficiaries of the trust upon request.

[244] Despite arguing that 690174 owed only limited fiduciary duties as a bare trustee, the Trustee argues that 690174 had full authority to subdivide Lot 1 and transfer title to the subdivided lots to purchasers. These submissions are inconsistent. More importantly, they ignore the fact that 690174 used its registered title to take steps that profoundly affected the beneficial ownership rights of the 2007 Joint Venturers.

[245] 690174 not only held title to Lot 1 in trust but also undertook the responsibility to apply for all necessary permits required for the development and subdivision of Lot 1. It is clear that by virtue of holding legal title to Lot 1, 690174 had the ability to affect the rights of all of the 2007 Joint Venturers. This made them vulnerable to the actions of 690174. The elements necessary to establish both an *ad hoc* fiduciary duty (as set out in more detail at para. 474 of these reasons) and a *per se* fiduciary duty on 690174 were therefore present in this case.

[246] The fiduciary duties owed by 690174 and Jaswant extended to all dealings with Lot 1 that could have affected the 2007 Joint Venturers' beneficial ownership of that lot. They also extended to all steps taken to pursue the commercial objective of the 2007 JVA, which was to subdivide Lot 1 for the benefit of the 2007 Joint Venturers.

Breaches of duty by 690174 and Jaswant

[247] As fiduciaries, 690174 and Jaswant were required to act honestly, in good faith, and in the best interests of the 2007 Joint Venture when exercising the powers they held by virtue of their position. This duty extended to avoiding any action that resulted in an unauthorized benefit to themselves and to obtaining the fully informed consent of the members of the 2007 Joint Venture prior to the taking of any action pursuant to those powers that could adversely affect them.

[248] I find that 690174 and Jaswant undertook a number of actions that breached those duties, including the following:

1. Permitting financial charges that arose from 690174's outside dealings to be registered against Lot 1.

2. Registering other financial charges against Lot 1 to provide security for obligations incurred by 690174 in pursuit of its separate business interests.

3. Purporting to transfer the beneficial ownership of Lot 1 to the members of the November 2010 and 2011 Joint Ventures.

4. Entering into the Land Swap Agreement, which transferred a significant portion of Lot 1 to the Anglican Diocese of New Westminster in exchange for land that was utilized for the benefit of the 2011 Joint Venturers without obtaining the informed consent of the 2007 Joint Venturers.

5. Executing a mortgage over Lot 1 to secure the WSCU financing that was used to finance the Project for the exclusive benefit of the 2011 Joint Venturers.

[249] The result of 690174's actions was to put the beneficial ownership of Lot 1 at risk and to receive benefits for themselves from Lot 1 that they had no right to obtain.

[250] 690174 could only have taken these steps if it had first obtained the informed consent of the 2007 Joint Venturers or undertaken them for the benefit of the 2007

Joint Venture. There is no evidence that 690174 obtained the necessary consent or that it was acting on behalf of the 2007 Joint Venture in carrying out the actions described above. To the contrary, Jaswant sought to justify his actions by testifying that Mr. Garcha had told him that he wanted nothing further to do with the 2007 Joint Venture, an issue I will deal with in the discussion of other defences to the Garcha Action.

[251] The record is also devoid of any evidence that, in their dealings with Lot 1, Jaswant or 690174 considered that they owed any duty whatsoever to the 2007 Joint Venturers. The evidence all suggests the opposite. Jaswant personally and through his companies acted solely in his own interests without any regard for the impact of his actions on the rights of the 2007 Joint Venturers.

[252] I am satisfied that these breaches were dishonest. As stated in *Air Canada v. M & L Travel Ltd.,* [1993] 3 S.C.R. 787 at 825-826*,* set out below at para. 289 of these reasons, any action by a fiduciary that exposes the beneficiary to a risk that the fiduciary is not entitled to take is a dishonest breach of duty.

Discussion of breaches by Jaswant and 690174

The Gill Judgment

[253] I have set out the circumstances that led to the registration of the Gill Judgment in paras. 159-166 above.

[254] 690174's duty as a trustee was to protect the title to Lot 1 and to utilize its own resources to clear charges registered against it arising out of its separate business activities. However, Jaswant concealed the registration of the Gill Judgment from the 2007 Joint Venturers and prevented them from taking steps to protect their beneficial ownership of Lot 1.

The Virk Mortgage

[255] I will deal with the Virk Mortgage here even though it occurred later than some of the other breaches I will address below. I do so because it is directly related to the Gill Judgment. I find that 690174 and Jaswant breached their fiduciary duties

by entering into the Virk Mortgage and charging Lot 1 as security for the separate obligations of 690174.

[256] Encumbering Lot 1 with the Virk Mortgage was both a breach of the express terms of the 2007 JVA and breach of the fiduciary duties owed to the 2007 Joint Venturers. It was a dishonest breach because it subjected Lot 1 to a risk that 690174 was not entitled to expose it to. While it provided Jaswant and 690174 with the opportunity to pursue the objects of the 2011 Joint Venture, it was of no benefit to the 2007 Joint Venturers who had been excluded from participation in the Project by the terms of the November 2010 and 2011 JVAs.

[257] I find that Jaswant wished to conceal his actions with respect to the Project and Lot 1 from the members of the 2007 Joint Venture because he was aware that he had granted security over Lot 1 for a debt that 690174 used to meet its separate obligations. I also infer from his actions that he was aware that he had not taken the steps necessary to protect the position of the 2007 Joint Venturers as beneficial owners of Lot 1.

[258] The subsequent release of funds provided by the Virk Mortgage to settle Mr. Gill's judgment allowed 690174 to proceed with subdivision of Lots 1 to 5 and to complete the financing for the Project from WSCU. However, it also burdened the beneficial owners of Lot 1 with a mortgage of approximately $1,000,000 which increased to more than $1,600,000 by the time it was paid. There can be no question that the granting this mortgage over Lot 1 was a dishonest breach of fiduciary duty on the part of Jaswant and 690174.

The November 2010 and 2011 JVAs

[259] 690174 and Jaswant also breached their fiduciary duties by entering into the November 2010 JVA and the 2011 JVA. Pursuant to para. 2.2 of the November 2010 JVA, Jaswant and 690174 agreed that Lot 1 would henceforth become part of the assets of that joint venture and would thereafter be beneficially owned by the November 2010 Joint Venturers according to their proportionate shares.

[260] In para. 3.3 of the November 2010 JVA, 690174 and Jaswant agreed that the net revenue from the November 2010 Joint Venture would be divided proportionately among the November 2010 Joint Venturers without making any provision to protect the 2007 Joint Venturers' beneficial ownership of Lot 1.

[261] In para 4.2, 690174 and Jaswant agreed that each of the November 2010 Joint Venturers owned, as their separate property, an undivided beneficial interest in Lots 1 to 5 in the ratio of its proportionate share. By executing the November 2010 JVA, 690174 had therefore purported to convey a beneficial interest in Lot 1 to each of the other November 2010 Joint Venturers. However, 690174 was not the beneficial owner of Lot 1.

[262] These provisions continued in force after the execution of the 2011 JVA.

The Land Swap Agreement

[263] The Land Swap Agreement was executed by the 2011 Joint Venturers on or about January 1, 2012. It clearly benefitted the members of that joint venture by facilitating a more profitable subdivision plan. By that time, it is clear that Jaswant and 690174 no longer considered themselves bound by the terms of the 2007 JVA.

[264] It is obvious that the execution of the Land Swap Agreement was a "Major Decision" affecting the members of the 2007 Joint Venture, as that term is defined in the 2007 JVA, because it resulted in the alienation of a significant portion of Lot 1. Despite this, Jaswant made no effort to obtain any consent from any 2007 Joint Venturer. I find that the execution of the Land Swap Agreement was one of the things that Jaswant had in mind when he told Mr. Morton that he did not want to disclose his legal affairs to the members of the 2007 Joint Venture.

[265] The Trustee submits that the Land Swap Agreement did not cause any loss to the 2007 Joint Venturers because it was a prudent step in the process of achieving a subdivision in all of the Lots in the Project.

[266] I do not accept this submission. The execution of the Land Swap Agreement without the informed consent of the 2007 Joint Venturers deprived them of the

opportunity to take any steps to protect their position in the Project. I have no doubt that a fully informed 2007 Joint Venturer who received legal advice regarding the Project in January 2012 would have insisted that their position be protected either by becoming a registered owner of a proportionate interest in the Project or by some other effective means.

[267] In any event, the law is clear that it is no answer for a fiduciary who has benefited from a breach of fiduciary duty to say that its actions caused no damage to the beneficiary. The obtaining of an unauthorized benefit is sufficient to establish liability in such circumstances.

The WSCU Financing

[268] 690174 and Jaswant also breached their duties by negotiating the terms of, and charging Lot 1 with, the WSCU mortgage charges. The first advance under the WSCU financing was used to pay off the outstanding balances on all of the Acquisition Mortgages. While those mortgages included the mortgage on Lot 1, they also included mortgages on all of the other Lots. As with the other breaches I have identified, the WSCU Mortgage required the informed consent of the 2007 Joint Venturers to affect their rights. Paragraph 7.3 of the 2007 JVA expressly states that the acceptance of a financing commitment required the prior written approval of all 2007 Joint Venturers. 690174 made no attempt to obtain such approval. The failure of 690174 and Jaswant to seek approval of the WSCU financing deprived the 2007 Joint Venturers of another opportunity to protect their rights under the 2007 JVA.

The subdivision

[269] Upon registration of the Land Swap Agreement and the subdivision plans, title to all of the subdivided lots was registered in the name of one or more of the 2011 Joint Venturers.

[270] The subdivision of Lots 1 to 5 and registration of the titles of those lots in the names of the 2011 Joint Venturers was a further breach of fiduciary duty because it permitted the Project to be completed for the sole benefit of the 2011 Joint Venturers. In this regard it is significant that the Trustee based his conclusion that

the 2007 Joint Venturers were equity creditors at least in part on the fact that they had no registered interest in the subdivided lots. While I do not agree that the Trustee was correct in so doing, there can be no doubt that the state of the registered title to the Project Lands caused actual harm to the 2007 Joint Venturers. Even on the Trustee's view of this matter, they would have been entitled to share in the proceeds of sale if their beneficial interest had been registered in the Land Title Office. That was the basis on which the Trustee decided that the 2011 Joint Venturers were not equity claimants.

Cumulative assessment of the breaches

[271] The cumulative effect of the numerous breaches of fiduciary duty was that the 2007 Joint Venturers were deprived of their beneficial ownership of Lot 1 and that the 2011 Joint Venturers have appropriated that benefit. As I will address later in the remedy section of these reasons, that is a result that a court of equity cannot permit.

[272] The Trustee has not been able to articulate any legal basis justifying 690174's actions in appropriating Lot 1 for its own benefit. In simple terms, 690174 did not own Lot 1. It had no right to transfer title to Lot 1 except at the direction of the 2007 Joint Venturers.

[273] The circumstances of these proceedings raise issues similar to those considered by the House of Lords in *Foskett v. McKeown,* [2000] 3 All E.R. 97, which addressed the nature of persons' interests in property they beneficially own but to which they have entrusted a Trustee or agent with legal title.

[274] In *Foskett*, an individual named Murphy promoted a plan to sell plots of land in Portugal. The purchase monies paid by purchasers were held in trust by Mr. Murphy pending the completion of the lots. Two years after the purchasers paid their money, it was learned that Mr. Murphy had dissipated it, in part by paying premiums on a life insurance policy of £1,000,000, of which his children were the beneficiaries. After the fraud was discovered Mr. Murphy committed suicide and, because the policy had been in force long enough to become payable in such an event, the beneficiaries were entitled to the death benefit.

[275] A dispute arose as to how the death benefit should be distributed. The precise question was whether the purchasers whose money was used to pay the premiums were entitled to share the death benefit pro rata with the children based on the relative amounts paid by Murphy out of his own funds and from the purchaser's money, or the purchasers were restricted to having a lien on the death benefit for repayment of the money of which they had been defrauded. A majority of the Law Lords held that the death benefit should be divided proportionately based on the respective contribution to the premiums from Murphy's own money and the purchasers' money.

[276] What makes *Foskett* relevant to the Garchas' claim is the analysis of the majority that concluded that the purchasers' claim was not based on unjust enrichment but on the right they had to follow their own property into the death benefit.

[277] This principle is explained in the reasons of Lord Browne Wilkinson in *Foskett* at 101-102:

> The crucial factor in this case is to appreciate that the purchasers are claiming a proprietary interest in the policy moneys and that such proprietary interest is not dependent on any discretion vested in the court. Nor is the purchasers claim based on unjust enrichment. It is based on the assertion by the purchasers of their equitable proprietary interest in identified property.
>
> The first step is to identify the interest of the purchasers: it is their absolute equitable interest in the moneys originally held … on the express trusts of the purchasers trust deed. This case does not involve any question of resulting or constructive trusts. The only trusts at issue are the express trusts of the purchasers trust deed. Under those express trusts the purchasers were entitled to equitable interests in the original moneys paid … by the purchasers. Like any other equitable proprietary interest, those equitable proprietary interests under the purchasers trust deed which originally existed in the moneys paid … now exist in any other property which, in law, now represents the original trust assets. If, as a result of tracing, it can be said that certain of the policy moneys are what now represent part of the assets subject to the trusts of the purchasers trust deed, then as a matter of English property law the purchasers have an absolute interest in such moneys. There is no discretion vested in the court. There is no room for any consideration whether, in the circumstances of this particular case, it is in a moral sense "equitable" for the purchasers to be so entitled. The rules establishing equitable proprietary interests and their enforceability against certain parties have been developed over the centuries and are an integral part of the property law of England. It is a fundamental error to think that, because certain property rights are equitable rather than legal, such rights are in some

> way discretionary. This case does not depend on whether it is fair, just and reasonable to give the purchasers an interest as a result of which the court in its discretion provides a remedy. It is a case of hard-nosed property rights.

[278] In my view, the above comments apply equally to the 2007 Joint Venturers. They were at all times the beneficial owners of Lot 1 and are entitled to trace their property into the proceeds of sale of the subdivided lots that are attributable to the contribution of Lot 1 to the Project.

[279] Thus, I find that the 28.5% share of the 2011 Joint Venture obtained by 690174 is beneficially owned by the 2007 Joint Venturers. There is a direct and clear path from the ownership of Lot 1 into 690174's 28.5% share of the 2011 Joint Venture. No other person acquired any interest in that share of the 2011 Joint Venture.

[280] This means that it is unnecessary for the Garchas to establish unjust enrichment or any other discretionary remedy. Their remedy is the right to recover their own property, which they have never lost.

[281] The Trustee made a number of submissions to the effect that Jaswant's pursuit of the Project did not cause any damage to the 2007 Joint Venture. Rather, the Trustee says that Jaswant's actions enhanced the value of Lot 1. However, the issue is who should have received the benefit of any such enhancement. In my view there can be only one answer to that question. The beneficial owners of Lot 1 were exclusively entitled to the benefit of its development. However, as a result of Jaswant's and 690174's actions they have been excluded entirely from receiving any benefit from Lot 1. It is difficult to conceive of a clearer example of a breach of fiduciary duty than the acts of Jaswant and 690174 in this case.

[282] In the above paragraphs I have made frequent references to the lack of informed consent on the part of the 2007 Joint Venturers to various steps taken by Jaswant and 690174. In so doing I have not overlooked the evidence that some of the 2007 Joint Venturers were aware that Lot 1 would be incorporated into a larger subdivision. However, there is simply no evidence that the Garchas or indeed any other 2007 Joint Venturer, gave their fully informed consent to the actions of 690174

and Jaswant that I have outlined above. The onus of establishing such consent is on 690174 and Jaswant. Even if one accepts Jaswant's evidence about Mr. Garcha's statements, which I do not, these defendants have failed to establish that they had the informed consent of the 2007 Joint Venturers to their actions.

Knowing Assistance and Knowing Receipt

[283] The Garchas submit that all of the members of the November 2010 Joint Venture hold their interests subject to a constructive trust in favour of the 2007 Joint Venturers based on knowingly assisting or knowingly receiving a benefit from 690174's and Jaswant's breaches of fiduciary duty.

[284] I have concluded that the appropriate remedy to be granted to the Garchas is their proportionate share of 690174's 28.5% share of the net revenue from the Project. In one sense this makes it unnecessary to consider the claims of knowing assistance and knowing receipt.

[285] However, I will address these claims for two reasons. The first is that if I am in error in concluding that the Garcha's claims are not equity claims postponed to the claims of all other creditors, the Garchas would still have a claim against the non-bankrupt defendants to satisfy their claims.

[286] Secondly, a finding of knowing assistance or knowing receipt would make the other defendants jointly and severally liable for the Garchas' claim. Thus, even if the Garchas' claim is not an equity claim, an issue will arise with respect to how the burden of their remedy should be borne as between the defendants who are found to be liable.

[287] Knowing assistance in, and knowing receipt of the benefit of, a breach of trust or fiduciary duty are related but distinct causes of action. I will therefore address them separately.

Knowing assistance

[288] A person who assists another in a breach of fiduciary duty may become liable to the beneficiary to the same extent as the person who committed the actual

breach. For a person to be liable for knowing assistance, they must have actual knowledge of the wrongful conduct of the defaulting fiduciary and knowingly assist in it. Imposition of liability requires that the wrongdoer's breach of fiduciary must be dishonest. A person can be liable for knowing assistance without receiving any benefit from its actions: *Air Canada* at 812.

[289] The issue in *Air Canada* was whether the directors of the defendant M & L Travel were liable for that company's breach of trust by putting funds which were held in trust for Air Canada into its general bank account, where they were subject to seizure by a bank. The Court held that by so doing M & L Travel took an impermissible risk that prejudiced the rights of the beneficiary, Air Canada, and therefore committed a dishonest breach of trust. At 825-826, Justice Iacobucci articulated the nature of the breach required in knowing assistance cases:

> 59 Where the trustee is a corporation, rather than an individual, the inquiry as to whether the breach of trust was dishonest and fraudulent may be more difficult to conceptualize, because the corporation can only act through human agents who are often the strangers to the trust whose liability is in issue. Regardless of the type of trustee, in my view, the standard adopted by Peter Gibson J. in the *Baden, Delvaux* case, following the decision of the English Court of Appeal in Belmont Finance, supra, is a helpful one. I would therefore "take as a relevant description of fraud 'the taking of a risk to the prejudice of another's rights, which risk is known to be one which there is no right to take'." In my opinion, this standard best accords with the basic rationale for the imposition of personal liability on a stranger to a trust which was enunciated in *In re Montagu's Settlement Trusts*, supra, namely, whether the stranger's conscience is sufficiently affected to justify the imposition of personal liability. In that respect, the taking of a knowingly wrongful risk resulting in prejudice to the beneficiary is sufficient to ground personal liability. This approach is consistent with both lines of authority previously discussed.

[290] Justice Iacobucci also referred to the decision of Justice Wilson of this court in *Scott v. Riehl* (1958), 15 D.L.R. (2d.) 67 (B.C. S.C.). In *Scott,* Justice Wilson held the directors of a small, closely-held company, who had used funds which were subject to a trust under the *Mechanics Lien Act*, *1956*, S.B.C. 1956, c. 27, for unauthorized purposes were equally liable with the company because they knew that all the monies that were deposited were subject to the trust and because they operated the account, drawing their salaries from it.

[291] In this case, the breaches I have found consist of dealing with Lot 1 in a manner that failed to recognize that the 2007 Joint Venturers were the beneficial owners of that lot. In my view the existence of the trust in favour of the 2007 Joint Venturers would have been obvious to anyone who read the 2007 JVA.

[292] All of the November 2010 and 2011 Joint Venturers participated in at least some the breaches I have identified by being parties to the agreements by which those breaches were brought about. None of these steps could have been taken without their participation and assistance.

[293] The real question therefore is which of the November 2010 and 2011 Joint Venturers, if any, had the requisite knowledge to be found liable on the basis of knowing assistance? When the wrongful act arises from the breach of a duty imposed under an agreement, the question of the assisters' knowledge will depend on the extent and familiarity they had with the agreement, although willful blindness may substitute for actual knowledge. Thus, to have the requisite knowledge, a November 2010 or 2011 Joint Venturer must be found to have had actual knowledge of the terms of the 2007 JVA or have been wilfully blind as to their existence.

[294] I have concluded that Panorama, Parmjit, Ranjit, and by extension Svender had actual notice of the terms of the 2007 JVA or were wilfully blind to its terms and are therefore liable for knowing assistance of Jaswant's and 690174's breaches.

[295] Panorama must have had actual knowledge of Jaswant's and 690174's breaches because Jaswant was the sole director and shareholder of Panorama and was its directing mind, as were the directors that Justice Wilson refers to in *Scott*. Panorama is therefore equally liable with 690174 and Jaswant based on knowing assistance.

[296] I find that Ranjit had actual notice of the terms of the 2007 JVA. Ranjit admitted that he saw the 2007 JVA in 2007. However, his counsel submits that there was no evidence that he was aware of the terms on which 690174 held title to Lot 1. I do not accept this submission. Ranjit was obviously an intelligent person with some experience in land development. His evidence at his examination for discovery was

that one of the two lots allocated to his close friend Joginder Chahal in the 2007 JVA was acquired on his behalf. He advanced money to Mr. Chahal on the basis of that arrangement. It is not credible to suggest that he would have entered into such a transaction without reading the underlying agreement that gave rise to that interest. I therefore find that Ranjit had the requisite knowledge or he was, at a minimum, wilfully blind to the terms of the 2007 JVA. Svender's counsel has conceded that he is equally liable with his father for any findings in this case. I therefore also find him liable for knowing assistance.

[297] I have already stated that I found Parmjit to be an unsatisfactory witness. I do not accept her evidence that she had virtually no knowledge of the details of her husband's business affairs even though she was a member of Sangha Groups 1 and 2 and of the November 2010 and 2011 JVAs. There is sufficient evidence to allow me to infer that Parmjit was very familiar with Jaswant's business and with the affairs of the various joint ventures in issue in these proceedings, including the terms of the 2007 JVA.

[298] I accept Jaswinder Garcha's evidence that in 2004 Parmjit asked her if she and her husband wished to invest in property development with Jaswant. Jaswant confirmed that this was the case in his evidence despite Parmjit's denial that any such discussion took place.

[299] Despite Parmjit's evidence that she looked after the home while her husband looked after the business, she signed numerous documents relating to Lot 1, including the first and second PMIC mortgages securing the refinancing of the IMOR mortgage on Lot 1. She gave her covenant for repayment of these mortgages and mortgaged her interest in Lot 2 to secure them. The Garchas were named parties to these mortgages. In addition, her sister was one of the 2007 Joint Venturers. Parmjit also struck me as a shrewd person. I do not find her evidence that she was unaware of the 2007 JVA to be credible. I find that she had actual knowledge of the terms of the 2007 JVA which stipulated that 690174 held legal title to Lot 1 in trust for the 2007 Joint Venturers, or at a minimum was wilfully blind to that fact.

[300] I also accept the submission of the Garchas' counsel that Parmjit is equally liable with Jaswant and 690174 on the principle referred to by Justice Southin in *Osborne v. Pavlick*, 2000 BCCA 120. *Osborne* was a case involving joint tortfeasors. A wife owned a business which was operated on a property owned jointly by herself and her husband, which they decided to sell as a package. The wife induced the plaintiffs to purchase the property by making fraudulent representations to them about the state of the business. The purchasers sued in fraud. At trial both the wife and husband were found liable on the basis that the wife was acting as the husband's agent in making the fraudulent representation.

[301] On appeal, Justice Southin concluded that it was not open to the trial judge to find that the wife was acting as the husband's agent in making the misrepresentation because no misrepresentation had been alleged against him. She did however find that the husband was liable as a joint tortfeasor with the wife, because they had embarked on a joint enterprise. She found that when two people engage in a joint enterprise and one commits a tort in carrying out the enterprise, both are liable for the tort.

[302] While *Osborne* was a tort case, the principle that persons involved in a joint enterprise can be found jointly liable for the wrongful acts of another was applied in a breach of fiduciary duty case: *Ruwenzori Enterprises Ltd. v. Walji et al.*, 2004 BCSC 741, *aff'd* 2006 BCCA 448. I can see no principled reason why it should not also apply in this case.

[303] I have no hesitation in finding that Parmjit and Jaswant were engaged in a joint enterprise, as explained in *Osborne*, with respect to the Project. Parmjit participated in Sangha Groups 1 and 2 and, according to her evidence, rolled her capital and profits from them into the Project. Parmjit became a member of the November 2010 and 2011 Joint Ventures. In all of these matters she was content to allow Jaswant to make all decisions with respect to the business and to benefit from those decisions.

[304] I also note that Parmjit alleged that she had advanced money to 690174 when she filed proofs of claims in that company's bankruptcy. This is a further

indication of Parmjit's close involvement in Jaswant's and 690174's business activities.

[305] The more difficult question is whether Wills and Dale are liable to the Garchas based on knowing assistance.

[306] Ms. Dale and Mr. Wills have not been shown to have actual knowledge of the terms of the 2007 JVA or any facts that suggested that 690174 was not the beneficial owner of Lot 1 at any material time. I accept their evidence that they did not know of the terms of the 2007 JVA and find no evidence from which I could draw a contrary inference. They are therefore not liable for knowingly assisting in Jaswant's and 690174's breaches of fiduciary duty.

[307] However, I have concluded that Wills and Dale are holding their interest in the 2011 Joint Venture as a nominee for Jaswant or 690174. With the possible exception of $25,000 advanced by them to 690174 on August 17, 2007, there is no documentary evidence showing that Wills or Dale contributed any funds to the Project or to the acquisition of Lots 1 to 5. The Trustee has concluded that the $25,000 advance was used to contribute to the deposit for the purchase of Lot 3. However, Wills and Dale's registered interest is in Lot 4. They therefore have made no contribution to the purchase of the Lot that constitutes their capital contribution to the 2011 Joint Venture.

[308] Ms. Dale and Mr. Wills testified that they began to invest in real estate projects being managed by Jaswant in the 1990s, and that the profits they had earned in earlier projects were rolled into the Project, ending with their acquisition of a half interest in Lot 4. However, they were unable to identify any specific projects in which they had invested. They could not say how much they invested or provide any proof of advances they made to any such project. They could produce no documents relating to any such investments. Jaswant's evidence was that Mr. Wills and Ms. Dale had been paid everything that they were entitled to from past projects and therefore had invested nothing in the Project.

[309] Wills and Dale also admitted that they had never declared any income from those previous projects on their tax returns. Their explanation for this was that they never actually received any funds from the projects. However, they produced no records or documents corroborating their evidence that they had earned any profits from them. They described themselves as being executives in multi-million-dollar enterprises. I find it difficult to accept that, as such, they were not aware of their obligation to disclose accrued income from these projects on their income tax returns.

[310] Ms. Dale did produce some handwritten notes showing receipt of net proceeds from the sale of three properties registered in her name in 2010. Two of these properties were sold to Ranjit and Joginder Chahal. It was not clear from the records who purchased the third property. Ms. Dale's notes record the receipt of the following net proceeds:

1. Lot 59	$62,814.97
2. Lot 60	$62,833.65
3. 58 Ave	$403,863.33

[311] The notes also indicate that a cheque of $403,690.62 was transferred to Jaswant's Coast Capital Account on an indecipherable date, probably in 2010. Ms. Dale also produced copies of a $25,000 bank draft to Jaswant which appears to be dated April 7, 2010, a $20,000 cheque to Jaswant dated May 5, 2010, and a $411,420.86 bank draft to Best Quality Homes Ltd. on July 29, 2011.

[312] However, the evidence shows that Best Quality Homes Ltd. provided the funds to purchase these properties and that the net proceeds of sale were paid to that company or to Jaswant. I conclude that Wills and Dale held title to those properties as a nominee for Best Quality Homes Ltd. or Jaswant.

[313] I also find that Jaswant had agreed that some consideration would be provided to Wills and Dale for providing their covenants on the financing for Lot 4 but that the amount of that consideration was never determined.

[314] As I understand the answers Jaswant gave under cross-examination, his evidence was that 690174 had provided all of the funds used to acquire Lot 4 and that he intended to recover those amounts from the profits earned from the Project before Wills and Dale were entitled to receive anything. I do not agree with Mr. Taylor that Jaswant's evidence was that all of the profits from Wills and Dale's proportionate interest would be paid to 690174. However, there was no evidence as to how much they would receive from the Project. What is clear is that Jaswant considered that he had the unilateral right to decide how much they would receive.

[315] According to the Ninth Report of the Trustee, 690174 advanced $488,227.53 towards the acquisition of Lot 4. The most recent information contained in Exhibit 175 showed a balance of $1,832,266.24 in the Vendor Trust Account set up in the name of Jaswant, Wills, and Dale, of which Wills and Dale are notionally entitled to a 50% interest. This means that they are asserting the right to receive over $900,000 from an investment of at most $25,000.

[316] Based on all of the forgoing I have concluded that Wills and Dale held their interest in Lot 4 as a nominee for 690174 or Jaswant. I find that they provided their covenants on the Acquisition Mortgage for Lot 4 to assist Jaswant to obtain that financing but that they did not have a beneficial ownership interest in that Lot. I find that there was an understanding that Wills and Dale would receive some compensation for giving their covenants for payment but that they had not agreed with Jaswant on the amount of that compensation by the time of his bankruptcy.

[317] Therefore, Wills and Dale are in the position of volunteers with respect to their interest in the Project and hold their interest subject to the Garchas' proprietary claim. However, they are not jointly liable with 690174 and Jaswant on the basis of knowing assistance.

[318] I have also concluded that Grewal Management did not have the required knowledge of the 2007 JVA to be liable for knowing assistance of 690174's breaches fiduciary duty, some of which occurred before Grewal Management became a joint venturer. Grewal Management did not become an investor in the

Project until 2011. There is no evidence that Mr. Grewal had actual knowledge of the terms of the 2007 JVA at any material time.

[319] Similarly, I am unable to find a sufficient evidentiary basis for finding that Raveen had actual knowledge of the terms of the 2007 JVA or was willfully blind with respect to it. While I did not find Raveen to be a credible witness, I am unable to draw any inference that she had the requisite state of knowledge to make her liable for knowing assistance of Jaswant's and 690174's breaches.

[320] I am also of the view that the circumstances in which the assignment fee from 690174 to 688350 was handled did not result in any receipt of a benefit by 688350 or Raveen. I find that the assignment fee was paid to inflate the apparent purchase price paid for Lot 1 in order to maximize the amount of mortgage financing that could be obtained to purchase it. These circumstances do no credit to Jaswant or Raveen. However, they do not constitute any actionable wrong at the instance of the Garchas.

Knowing receipt

[321] The Garchas also claim against the 2011 Joint Venturers on the basis of knowing receipt.

[322] Knowing receipt is the receipt of property that is known to be subject to a trust or obtained through a breach of fiduciary duty. A person therefore cannot be liable for knowing receipt without actually having received some benefit obtained from the breach. However, unlike liability for knowing assistance, a person may be liable for knowing receipt on the basis of constructive notice of the fiduciary obligation.

[323] The requisite state of knowledge for knowing receipt is set out by Justice La Forest in *Citadel General Assurance Co. v. Lloyds Bank Canada*, [1997] 3 S.C.R. 805 at 836-837:

> 48 Given the fundamental distinction between the nature of liability in assistance and receipt cases, it makes sense to require a different threshold of knowledge for each category of liability. In "knowing assistance" cases, which are concerned with the furtherance of fraud, there is a higher threshold of knowledge required of the stranger to the trust. Constructive knowledge is excluded as the basis for liability in "knowing assistance" cases; see *Air*

> *Canada v. M & L Travel Ltd., National Westminster Bank Ltd.*, supra, at pp. 811-13. However, in "knowing receipt" cases, which are concerned with the receipt of trust property for one's own benefit, there should be a lower threshold of knowledge required of the stranger to the trust. More is expected of the recipient, who, unlike the accessory, is necessarily enriched at the plaintiff's expense. Because the recipient is held to this higher standard, constructive knowledge (that is, knowledge of facts sufficient to put a reasonable person on notice or inquiry) will suffice as the basis for restitutionary liability. Iacobucci J. reaches the same conclusion in *Gold v National Westminster Bank Ltd.*, supra, where he finds, at para. 46, that a stranger in receipt of trust property "need not have actual knowledge of the equity [in favour of the plaintiff]; notice will suffice".

[324] In this case it is clear that Panorama, through Jaswant, had actual knowledge of Jaswant's and 690174's breaches and, as set out above, received a benefit from the incorporation of Lot 1 into the Project. It is therefore also liable for knowing receipt of a benefit obtained by a breach of trust.

[325] As Ranjit benefited from 690174's breaches and had actual knowledge of the terms of the 2007 JVA, he is liable as a person in knowing receipt of a benefit. Even if he did not have actual knowledge, I am of the view that Ranjit's knowledge of and participation in the 2007 Joint Venture were sufficient to put him on notice and under a duty to make inquiries about the 2007 JVA. Ranjit admits that he had knowledge of the 2007 JVA. It is inconceivable that he did not know that the purpose of the 2007 JVA was to develop Lot 1 and that others had invested in it. The combination of receipt of property subject to a trust and being put on notice of facts requiring further inquiry is sufficient to impose liability on Ranjit for knowing receipt.

[326] As I have already stated, counsel for Ranjit and Svender conceded that Svender is bound by any finding made against his father. I therefore find Svender liable for knowing receipt as well.

[327] I find that at a minimum Parmjit was aware of sufficient facts to impose on her a duty to make further inquiries before taking a benefit from Lot 1. It is simply not credible for her to deny that she was not aware of the existence of the 2007 JVA. At a minimum, she must have known that Jaswant had entered into a joint venture agreement with other persons with respect to Lot 1. She was also aware that no reference was made to any of those persons in Jaswant and 690174's dealing with

Lot 1. These circumstances were sufficient to put her on inquiry before accepting an interest in Lot 1. Her failure to do so makes her liable for knowing receipt of property obtained by a breach of fiduciary duty.

[328] My findings with respect to Parmjit's liability for knowing assistance by virtue of being engaged in a joint enterprise with Jaswant apply equally to her liability for knowing receipt.

[329] Raveen certainly played an active role in relation to the Land Swap and subdivision of the 5 Lots. However, there is no evidence that she received any benefit from her involvement in these actions.

[330] I also find that the Garchas have not established that Raveen is liable to them as a *trustee de son tort.* A person may be found liable as a *trustee de son tort* if they assume trust duties over property even though they have not been appointed to the office of a trustee. The Garchas submit that when Raveen became the trustee of Lots 1 to 5 in connection with the Land Swap, she became a *trustee de son tort* to them. However, as I read the authorities, a person does not become a trustee of another person unless they are aware that the property over which they have control is held in trust for that person. In this case, I am not satisfied that Raveen knew that Lot 1 was being held in trust for the members of the 2007 JVA. Her duty was to the persons who appointed her as trustee, that is, the 2011 Joint Venturers. In the absence of actual knowledge of the trust on Raveen's part or of the receipt of any benefit from the trust property, Raveen cannot be liable as a *trustee de son tort.*

[331] Accordingly, I find that the Garchas have not established any claim against Raveen in these proceedings.

[332] Because I am of the view that the appropriate remedy for the Garchas is to declare that they are entitled to their proportionate share of 690174's 28.5% interest in the 2011 Joint Venture it is not necessary for me to make any award against the other 2011 Joint Venturers whom I have found liable for knowing assistance or knowing receipt.

[333] I therefore simply make a declaration that those joint venturers knowingly assisted 690174's breaches and knowingly received a benefit from the breaches.

[334] At trial, 690174 made no submissions with respect to how any award made in favour of the plaintiffs should be allocated among the defendants. No defendant advanced any claim for indemnity or contribution against any other with respect to any such award. The position taken by the defendants was that the plaintiffs' claims were without merit and ought to be dismissed, or, in the case of the Trustee, that any claims were equity claims that were subordinated to the claims of all other creditors of the Bankrupts. Given these positions, I am unable to grant any relief in favour of any defendant against any other defendant at this time.

[335] However, I am prepared to receive submissions on this question once the defendants have had the opportunity to assess their positions in view of the findings I have made in favour of the plaintiffs. Such submissions should be made at the same time as the Accounting Hearing referred to at para. 618.

Affirmative Defences Raised by Defendants in the Garcha Action

The defence of election

[336] The Trustee, Raveen, and Parmjit submit that the Garchas have elected a remedy inconsistent with the claims they advance for equitable relief and are thereby precluded from obtaining that relief.

[337] In their notice of civil claim, the Garchas advanced the claim for equitable remedies flowing from the breaches of fiduciary duty that I have addressed above. However, Mr. Garcha also claimed judgment against 690174 as the maker of the Promissory Note. Although this claim was contained in the notice of civil claim, it was made separately by Mr. Garcha and not as an alternative to the claims based on breach of equitable duties.

[338] In the Promissory Note, 690174 promised to pay Mr. Garcha the principal amount of $484,252 without interest. The Promissory Note recited that Mr. Garcha agreed and acknowledged that the principal amount represents Mr. Garcha's 2007 Joint Venture contribution paid to 690174 pursuant to the 2007 JVA and stated that

690174 was entitled to prepay any portion of the amount owing without notice, bonus, or penalty.

[339] 690174 did not deliver a response to the notice of civil claim, and on March 17, 2015, Mr. Garcha obtained a default judgment for the amount of the Promissory Note. Mr. Garcha then attempted to register that judgment against the interest of 690174 in the Project. Any enforcement proceedings on the judgment were of course stayed upon 690174's bankruptcy.

[340] On November 9, 2018 the Trustee filed a response to the Garchas' notice of civil claim, pursuant to the order of Justice Bowden dated June 26, 2018, that granted it leave to defend this action on behalf of the Bankrupts.

[341] The Trustee did not plead that the Garcha's right to pursue the action was barred by the doctrine of election or the principles of issue estoppel in his original response to civil claim. He did however plead that the acceptance of the Promissory Note amounted to what was in effect an accord and satisfaction of the Garchas' claims.

[342] In their amended response to civil claim filed January 17, 2019, Parmjit and Raveen did not raise the defence of election or merger, but they pleaded that the Garchas' claims "have been limited by the promissory note given 690174 BC Ltd and taken by the Plaintiffs". This plea remained unchanged in the amended response to civil claim dated February 21, 2020, in response to the Garchas' amended notice of civil claim, filed by leave of the court on January 28, 2020. To the extent that this is a good pleading, I find that it also was a plea of accord and satisfaction.

[343] The Trustee did, however, raise what could be characterized as the defence of merger in para. 1 of Part 3 of its February 24, 2020, amended response to civil claim, which also responded to the Garchas' amended notice of civil claim. That pleading states "having taken the default judgment, the Plaintiffs are barred from suing further as against 690174 as any other cause of action they had as against 690174 was merged in the default judgment".

[344] I note that this pleading was contained in a pleading filed in response to the Garchas' amended notice of civil claim. The Trustee did not apply for leave to amend, but was entitled to amend to meet the new matters raised in the Garchas' amendment pursuant to Rule 6-1(5)(a) of the *SCCR*. However, this portion of the Trustee's amendment did not respond to any new matter raised by the Garchas' amendment. It would therefore appear that this pleading was not authorized under the *SCCR*.

[345] The Garchas have not raised any objection to the defence of election being relied upon by the defendants. While I have some doubt about whether it was open to Parmjit and Raveen to rely on the doctrine of election or for the Trustee to raise this defence for the first time in its amended response to civil claim, I will nevertheless address that defense in these reasons.

[346] The Trustee argued that the taking of a default judgment constituted an irrevocable election by Mr. Garcha to recover his investment through the personal judgment on the Promissory Note to the exclusion of any other remedy. The Trustee relies on *Ladner v. Ladner*, 2004 BCCA 366, and *H.Y. Louie Co. Limited v. Bowick*, 2015 BCCA 256, for the proposition that a party who elects to take one remedy for a cause of action is precluded from seeking an alternative remedy at a later time.

[347] There is no question that a party who pursues alternative remedies for the same cause of action must at some point elect which remedy it seeks from the court. The law is equally clear that such an election need not be made before judgment. However, a party may obtain concurrent remedies at different times or in separate proceedings.

[348] A plaintiff who takes judgment for an alternative remedy is precluded from pursuing the other remedy by virtue of the doctrine of election unless the dictates of fairness and justice require a second action: *Ladner* at para. 47. Recent jurisprudence also suggests that the doctrines of merger and election are closely related to the principles of *res judicata*, issue estoppel, and cause of action estoppel, and that the underlying rationale for all of these doctrines is preventing abuse of the court's process.

[349] Election applies only when the plaintiff is seeking to enforce the same cause of action. A cause of action is a factual situation giving rise to a claim or remedy: *Ladner* at para. 49; *Letang v. Cooper*, [1965] 1 Q.B. 232 (Eng. C.A.) at 242-3. Therefore, the threshold question is whether the Garchas are seeking to enforce the same cause of action on which Mr. Garcha took default judgment.

[350] In this case I am not satisfied that the Garchas are seeking a remedy for the same cause of action. Their claim for breach of trust and fiduciary duty is based on the manner in which 690174 and Jaswant discharged their trust and fiduciary duties to the members of the 2007 Joint Venture. Mr. Garcha's judgment is based on the Promissory Note, which was made well after the breaches of fiduciary duty. There is clearly a connection between the two claims. However, it is also clear that either claim could have been advanced independently of the other, that is, without relying on any of the facts giving rise to the other claim. This is so because a promissory note creates a cause of action independent of any underlying obligation.

[351] Subject to the issue of election and merger, the acceptance of the Promissory Note and the obtaining of judgment on it would bar any further claim for breaches of equitable duty only if the Promissory Note was given and accepted in satisfaction of the Garchas' claims for relief arising out of those claims. Whether that occurred is a question of fact. In this case there was no evidence that the Promissory Note was given or accepted in full satisfaction of the Garchas' claims. Neither Jaswant nor Mr. Garcha testified that that was the case. The Promissory Note does not clearly state that the note was intended to be a full settlement of the Garchas' claims.

[352] In addition, the circumstances under which Mr. Garcha took judgment on the Promissory Note are inconsistent with his having accepted it in full satisfaction of his claim. The Garchas continued to pursue equitable relief after Mr. Garcha received the Promissory Note and after Mr. Garcha took judgment.

[353] I therefore conclude that the defendants have not established that the Garchas have elected to accept the Promissory Note in satisfaction of their claims.

[354] The alternate question is whether the doctrine of election applies to preclude the Garchas from seeking to claim a property interest in the Project. This in turn depends on whether the remedies sought by the Garchas are alternative or cumulative. If they are alternative, any further claim may be barred by the doctrine of election, while if they are cumulative they are not. However, I am also satisfied that even if they are alternative, I am required to consider whether allowing the action to continue would be an abuse of the court's process or whether it is in the interests of justice to allow it to proceed.

[355] If the default judgment is viewed as a remedy for 690174's breaches of trust and fiduciary duty, it is clearly a personal or *in personam* remedy. The question is whether such a personal remedy against a defaulting fiduciary is inconsistent with continuing to seek an equitable remedy through a charge on the assets that it has misappropriated.

[356] In *Bronson v. Tompkins Ranching Ltd.*, 2012 BCSC 770, Justice Gropper succinctly summarized the principle that a wronged person alleging a breach of fiduciary duty may pursue personal remedies against the wrongdoer and seek a charge against the proceeds of the wrongdoing because these remedies are cumulative.

> 93 The two remedies in the case at bar are: (a) an *in personam* remedy against the trustee; and (b) an in rem remedy against the misappropriated trust property. Ultimately, the conclusion as to whether these remedies are alternative or cumulative is critical. If alternative, the plaintiffs are precluded from bringing the Second Action because they elected between the two remedies at the time of judgment in the First Action. If cumulative, the plaintiffs can bring the Second Action as they have not yet elected between the two remedies because they have not received full satisfaction for their loss.
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> 94 Framing the question differently, are the two remedies "inconsistent"? If yes, they are alternative. If no, they are cumulative. Other than the fact that the plaintiffs cannot have both remedies (as this would offend the rule against double satisfaction), there is no inconsistency between the two remedies.
>
> 95 There is English authority which states that an *in personam* claim against a defaulting trustee advanced in a first action may be supplemented in a later action by a claim to enforce an equitable charge or lien over the proceeds in which the misappropriated assets have been mixed. This is permitted because these remedies are cumulative: see *Serious Fraud Office v. Lexi Holdings Plc*, [2008] EWCA Crim 1443 (Eng. C.A.), at para. 39-40

> [*Serious Fraud Office*]. I note the Court in that case relied on *Tang Man Sit* to arrive at this conclusion. It seems to me that if pursuing an *in personam* claim against a defaulting trustee and pursuing an equitable charge over the misappropriated property are cumulative remedies, then it can equally be said that pursuing an *in personam* claim against a trustee for breach of trust and an in rem claim against the third party who has knowingly assisted in the breach of trust are cumulative remedies. Indeed, the latter is a remedy that could be characterized as one "in aid of" the remedy against the trustee: *Serious Fraud Office*, at para. 40.

[357] These considerations apply in this case. I find that the remedies sought by the Garchas are cumulative and that the doctrine of election therefore has no application.

[358] A somewhat similar situation arose in *Citadel General Insurance Co. v. Lloyd's Bank of Canada*, [1993] A.J. No. 680 (Alta. Q.B.). In that case the plaintiff insurance company alleged that the defendant bank was liable to it for knowing receipt of funds that its customer held in trust for the plaintiff. The funds in question were insurance premiums had been collected in trust for the plaintiff by the bank's customer. The customer was in financial difficulty and defaulted in paying over the premiums to the plaintiff after the defendant bank debited its bank account to cover overdrafts owing to it.

[359] When the customer defaulted in remitting the premiums, the plaintiff obtained a promissory note from it for the amount that it owed. The customer made some payments on the note but ultimately defaulted. The plaintiff sued on the note for the balance owing to it but was unable to collect anything in the action. From para. 11 of the reasons it appears that the plaintiff did take judgment on the note because that was the only way it could enforce it.

[360] The defendant bank argued that by accepting the note the plaintiff had revoked the trust or acquiesced in the use of the funds by the customer. The court rejected that argument and held that the plaintiff had merely asked for the note as confirmation of the amount owing to it. In the Supreme Court of Canada's 2007 decision in *Citadel General Insurance*, the Court agreed with the trial decision on this point.

[361] I find that the cases relied upon by the defendants are distinguishable.

[362] In *Ladner,* Justice Huddart recognized that the court has the discretion to allow a claim otherwise subject to the doctrine of election to proceed if it is in the interests of justice to do so:

> 50 This appeal comes, I think, to the question of whether, by entering judgment for damages, the appellant elected to forego her claim for an equitable remedy, and whether, if she did, there is reason in the record to allow the claim to proceed in any event, as there was in *Hoque v. Montreal Trust of Canada* (1997), 162 N.S.R. (2d) 321 (C.A.), leave to appeal to S.C.C. refused, [1997] S.C.C.A. No. 656.

[363] The facts of this case can usefully be compared to the facts in *Ladner*, as outlined in Justice Huddart's reasons:

> 51 Although not pleaded before Parrett J. and the Court of Appeal, the appellant sought to establish a constructive trust over the Canadian Bar Association policies. That claim was properly rejected. The appellant abandoned her claim for specific performance of the separation agreement, and sought no other equitable remedy over the three policies with which this appeal is concerned or any of the other estate assets. When she learned of the estate's alleged insolvency, the appellant did not seek to amend her pleadings, to allege a "good conscience" trust. Nor did she seek an adjournment of the hearing to assess damages so she might reconsider her position or attempt to lead new evidence. Scarth J. assessed damages; his order was entered and not appealed. After the order was interpreted in a manner unfavourable to her, the appellant did not apply to extend the time for appeal. No new material facts have since come to light.

[364] In *Ladner* there was an express finding that the appellant knowingly had foregone her claim to equitable relief. In this case, it is clear to me that the Garchas did not intend to forego their claim for equitable relief over the property of which they have been wrongfully deprived.

[365] In *H. Y. Louie*, the issue was the proper characterization of a judgment obtained against a defendant prior to the defendant's bankruptcy. The plaintiff alleged that it was entitled to pursue the defendant after bankruptcy because its claim against the defendant was for obtaining property by false pretenses. The majority of the British Columbia Court of Appeal held that the judgment had been obtained for breach of contract because it was the pleadings that determined the nature of the plaintiff's claim. In that case there was no issue about whether the

claims were concurrent or alternative. There had been only one claim made against the defendant. The plaintiff had consented to the judgment on that basis even though it was aware there was a possible claim for false pretenses

[366] As the above quotation from *Bronson* makes clear, the Garchas are not entitled to recover twice for the defendants' wrongdoing. Thus, if Mr. Garcha had recovered anything under the judgment, that amount would have to be taken into account in determining his remedy based on the rule against double recovery. However, that issue does not arise in this case because Mr. Garcha has not collected anything on the judgment.

[367] In addition, Jaswinder Kaur Garcha was not a party to the Promissory Note and did not take judgment on it. No question of election can therefore arise in respect of her claim.

[368] I have also concluded that I have the jurisdiction to allow the Garchas' claims for breach of trust and breach of fiduciary duty to be determined on the merits if it is in the interests of justice to do so.

[369] In *Tang Man Sit v. Capacious Investments Ltd*, [1995] UKPC 54, the Privy Council held that the doctrine of election was part of a general and overriding principle that legal proceedings should be conducted in a manner that strikes a fair and reasonable balance between the interests of the parties, having regard to the wider public interest in the conduct and finality of court proceedings. *Tang Man Sit* was cited with approval by Justice Gropper in *Bronson*.

[370] In *Danyluk v. Ainsworth Technologies Inc.*, 2001 SCC 44, Justice Binnie commented on the principle of issue estoppel that "the Court should stand back and, taking into account the entirety of the circumstances, consider whether application of issue estoppel in the particular case would work an injustice, considering the procedural and equitable issues at stake": at para. 80.

[371] In *Danyluk,* Justice Binnie also referred to the reasons of Justice Finch, as he then was, in *British Columbia (Ministry of Forests) v. Bugbusters Pest Management Inc.* (1998), 159 D.L.R. (4th) 50 (B.C. C.A.) at para. 32:

> It must always be remembered that although the three requirements for issue estoppel must be satisfied before it can apply, the fact that they may be satisfied does not automatically give rise to its application. Issue estoppel is an equitable doctrine, and as can be seen from the cases, is closely related to abuse of process. The doctrine of issue estoppel is designed as an implement of justice, and a protection against injustice. It inevitably calls upon the exercise of a judicial discretion to achieve fairness according to the circumstances of each case.

[372] Justice Binnie's closing comments on the nature of the court's discretion in applying issue estoppel are also relevant to this case:

> 66 In my view it was an error of principle not to address the factors for and against the exercise of the discretion which the court clearly possessed. This is not a situation where this Court is being asked by an appellant to substitute its opinion for that of the motions judge or the Court of Appeal. The appellant is entitled at some stage to appropriate consideration of the discretionary factors and to date this has not happened.
>
> 67 The list of factors is open. They include many of the same factors listed in *Maybrun* in connection with the rule against collateral attack. A similarly helpful list was proposed by Laskin J.A. in *Minott*, *supra*. The objective is to ensure that the operation of issue estoppel promotes the orderly administration of justice but not at the cost of real injustice in the particular case. …

[373] In *Minott v. O'Shanter Development Co.* (1999), 42 O.R. (3d) 321 (C.A.), Justice Laskin stated the proposition as follows at paras. 49-50:

> Even had the three requirements been met, however, in my view the court has always retained discretion to refuse to apply issue estoppel when to do so would cause unfairness or work an injustice. As Lord Upjohn observed in *Carl Zeiss Stiftung v. Rayner Keeler Ltd.*, [1967] 1 A.C. 853 at p. 947, [1966] 2 All E.R. 536, "[a]ll estoppels are not odious but must be applied so as to work justice and not injustice, and I think the principle of issue estoppel must be applied to the circumstances of the subsequent case with this overriding consideration in mind."
>
> Issue estoppel is a rule of public policy and, as a rule of public policy, it seeks to balance the public interest in the finality of litigation with the private interest in achieving justice between litigants. Sometimes these two interests will be in conflict, or at least there will be tension between them. Judicial discretion is required to achieve practical justice without undermining the principles on which issue estoppel is founded. Issue estoppel should be applied flexibly where an unyielding application of it would be unfair to a party who is precluded from relitigating an issue.

[374] I am aware that many of these cases involve decisions of tribunals and that the issue before the Court was whether the doctrine of issue estoppel barred a

further action. However, the English authorities referred to by Justice Gropper in *Bronson* have held that there is a general rule that the overriding question is whether pursuing a claim after judgment arising out of the same facts constitutes an abuse of process.

[375] I conclude that the interests of justice require that the court permit the Garchas' claim for equitable relief to continue even if the elements of election applied to Mr. Garcha. From the outset of these proceedings the Garchas have asserted a beneficial interest in the proceeds of the sale of Lot 1. I find that it would be unfair to deny them a remedy because Mr. Garcha took default judgment on the Promissory Note.

[376] The evidence at trial shows that 690174 and Jaswant have benefitted to a considerable degree from their wrongful acts. They have had the opportunity to dispute their liability and through the Trustee have done so.

[377] I also rely on the fact that 690174 stood in the position of a fiduciary to the Garchas at the time that Jaswant presented the Promissory Note to Mr. Garcha. As a fiduciary, 690174 owed a duty to make full disclosure of all relevant circumstances concerning the note to Mr. Garcha. There is no evidence that Jaswant informed Mr. Garcha that it was unlikely that 690174 was or would be in a position to honour the Promissory Note if it was presented for payment. In particular, 690174 presented the note after Ms. Virk commenced foreclosure proceedings against the Project and after the Grewal Action had been commenced. By that time, it was unlikely that 690174 could honour the Promissory Note.

[378] In addition, at the time the Mr. Garcha's counsel took default judgment, the facts relating to Jaswant's conduct, the degree to which funds had been mixed by Jaswant, and the numerous inconsistent agreements that the Jaswant-controlled parties had entered into had not been fully explored.

[379] Finally, if the plea of election is given effect, Mr. Garcha will be deprived of the beneficial interest he owns in Lot 1 despite having contributed a significant amount to its acquisition.

[380] The last part of the relevant analysis considers whether allowing the Garcha claim to continue would be to permit an abuse of the process of the Court. In my view it would not. On the contrary, it is my view that the consequences of applying the doctrine of election to preclude the Garchas obtaining the relief to which I have found they are otherwise entitled would result in an injustice.

[381] I therefore conclude that the default judgment is not a bar to the claims pursued by the Garchas at trial.

Defence of non-compliance with subdivision requirements of the *LTA*

[382] Parmjit and Raveen submit that the version of the oral agreement that Mr. Garcha testified to, one in which the Garchas would receive seven subdivided lots, offends s. 73 of the *Land Title Act*, R.S.B.C. 1996, c. 250 [*LTA*], because it amounts to a subdivision of Lot 1 without complying with the requirements of the *LTA* for subdivision. In *International Paper Industries Ltd. v. Top Line Industries Inc.* (1996), 20 B.C.L.R. (3d) 41 (B.C. C.A.), the Court of Appeal held that an agreement to lease a portion of un-subdivided land to a tenant without complying with the subdivision requirements of the *LTA* was void and unenforceable. Parmjit and Raveen say that this decision precludes the Garchas from asserting any claim to have lots transferred to them.

[383] As I understand it, this argument does not assert that the express terms of the 2007 JVA violate s. 73. Rather, it is directed to Mr. Garcha's subjective understanding of the agreement he made with Jaswant as set out in the Garchas' further amended notice of civil claim. However, I have already decided that the Garchas are bound by the terms of the written 2007 JVA and that their rights must be determined on that basis, without regard to their subjective understanding of the agreement.

[384] Therefore, I find that s. 73 of the *LTA* has no application to the enforceability of the 2007 JVA, which clearly contemplates that any subdivision will be carried out in accordance with all applicable legislative requirements.

Repudiation or fundamental breach of 2007 JVA by the Garchas

[385] The Trustee and Parmjit argue that the Garchas "walked away" from the 2007 Joint Venture and that this justified Jaswant's actions in dealing with Lot 1 without regard to their interests.

[386] It is not clear whether this argument asserts that the Garchas repudiated the 2007 JVA or that they were in fundamental breach of their obligations under it, although these terms are sometimes used interchangeably. These concepts apply only to executory contracts. The Garcha's claims are based on their beneficial ownership of their proportionate share of Lot 1. It is therefore questionable whether they apply in this case. In any event, the evidence does not establish either ground for 690174 failing to carry out its obligations under the 2007 JVA.

[387] A party repudiates a contract when it communicates an unequivocal intention to no longer be bound by it. A party can therefore repudiate a contract without actually breaching any performance obligation up to the time of repudiation. Fundamental breach occurs when a party breaches a contract in such a way as to deprive the innocent party of any benefit from the contract.

[388] The law is well-settled that a party alleging that a contract has come to an end by virtue of a repudiation must demonstrate that the conduct of the other party evinced an unequivocal intention not to be bound by the terms of the agreement, and that the innocent party had accepted and communicated an acceptance of the repudiation to the party in breach: G.H.L. Fridman, *The Law of Contract in Canada*, 6th ed. (Toronto: Thomson Reuters Canada, 2011) at 585-6 [Fridman]; *Doman Forest Products Ltd. v. GMAC Commercial Credit Corp. Canada*, 2007 BCCA 88.

[389] The elements necessary to establish a fundamental breach were set out by Justice Wilson in *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426 at 499-500:

> 148 The formulation that I prefer is that given by Lord Diplock in *Photo Production Ltd. v. Securicor Tpt. Ltd.*, [1980] A.C. 827, [1980] 2 W.L.R. 283, [1980] 1 All E.R. 556 (H.L.). A fundamental breach occurs "Where the event resulting from the failure by one party to perform a primary obligation has the effect of depriving the other party of substantially the whole benefit which it

> was the intention of the parties that he should obtain from the contract" (p. 849) (emphasis added). This is a restrictive definition and rightly so, I believe. As Lord Diplock points out, the usual remedy for breach of a "primary" contractual obligation (the thing bargained for) is a concomitant "secondary" obligation to pay damages. The other primary obligations of both parties yet unperformed remain in place. Fundamental breach represents an exception to this rule for it gives to the innocent party an additional remedy, an election to "put an end to all primary obligations of both parties remaining unperformed" (p. 849). It seems to me that this exceptional remedy should be available only in circumstances where the foundation of the contract has been undermined, where the very thing bargained for has not been provided.

[390] I do not agree that the Garchas “walked away” from their investment. The evidence relied upon by the Trustee in support of this argument consists of Jaswant’s testimony that Mr. Garcha told him he could “let it burn” when he asked Mr. Garcha for more contributions to the expenses of the 2007 Joint Venture and on the failure of the Garchas to make further contributions to the 2007 Joint Venture after October 2009.

[391] The evidence about the statement comes from Jaswant. Mr. Garcha denies making that statement. When Jaswant’s evidence conflicts with that of Mr. Garcha, I prefer Mr. Garcha’s evidence.

[392] In addition, I find that by October 2009, Jaswant had ceased to pursue the purposes of the 2007 Joint Venture, which contemplated the subdivision of only Lot 1. At that point, 690174 had no further right to ask for funds from the 2007 Joint Venturers without obtaining their informed consent to the incorporation of Lot 1 into the Project.

[393] While the Trustee argues that the 2007 Joint Venture was not incompatible with a larger subdivision, it clearly was incompatible with the manner in which the November 2010 JVA purported to divide up the beneficial ownership of the lands being subdivided.

[394] Apart from the evidence of Jaswant that I have rejected, there is no evidence that the Garchas ever refused to meet their obligations under the 2007 JVA. In any event, even if Jaswant’s evidence is accepted, it amounts to no more than an assertion that the Garchas refused to make further financial contributions to the

2007 Joint Venture. It is clear that Jaswant and 690174 did not comply with the procedures for raising funds set out in the 2007 JVA, and accordingly the Garchas were under no obligation to comply with his requests for further financial contributions.

[395] In this case, 690174 has continued to enjoy the principal benefit that it obtained from the 2007 JVA: the ability to utilize Lot 1 in the Project. It therefore has also failed to establish the elements necessary to establish fundamental breach.

[396] At worst, a failure to advance funds, assuming that the request was made in accordance with the parties' agreement, would constitute a default on the part of the party refusing to do so. The appropriate remedy for any such default would have been to take it into account upon division of the 2007 Joint Venture's proceeds. It might have also led to a claim for damages: *307527 B.C. Ltd. v. Cambridge*, 2003 BCSC 1027 at paras. 253-258.

[397] There is therefore no basis for concluding that the Garchas are precluded from a remedy on these grounds.

Effect of the order of Justice Harvey of May 19, 2015

[398] While it is not entirely clear, the Trustee's argument seems to be that the Harvey Order somehow extinguished the property rights of the 2007 Joint Venturers in Lot 1.

[399] The Trustee submits that the Garchas are bound by the Harvey Order because they are persons claiming by, through, or under 690174 and therefore are bound by the priority established in para. 8 of that order.

[400] However, I find that the Trustee has misapprehended the effect of the Harvey Order. That order was an order *nisi* of foreclosure declaring that the Virk Mortgage was a valid charge ranking in priority to the respondents in the property charged by the Virk Mortgage.

[401] There is no question that Ms. Virk was entitled by virtue of the priorities set out in the *LTA* to rely on the registered state of title to the lands charged by her

mortgage, including Lot 1, and to treat 690174 as the owner of Lot 1 for the purposes of establishing its priority.

[402] However, the Harvey Order merely established that the Virk Mortgage ranked in priority to the Garchas' interest in Lot 1. It did not in any way determine the validity of that interest, nor did it extinguish it or determine the rights of the parties to these proceedings against each other. To the contrary, an order *nisi* of foreclosure as a matter of law recognizes the right of persons whose interests rank behind the foreclosing mortgagee to redeem its mortgage.

[403] The Harvey Order is therefore irrelevant to the issues in this case, apart from being a step in a process that put the Garchas' beneficial ownership rights in Lot 1 at risk.

Effect of registration of an interest in the Land Title Office

[404] Wills and Dale rely upon on s. 23 of the *LTA*, arguing that it protected their registered title.

[405] Section 23 of the *LTA* provides as follows:

> 23 (1) In this section, "court" includes a person or statutory body having, by law or consent of parties, authority to hear, receive and examine evidence.
>
> (2) An indefeasible title, as long as it remains in force and uncancelled, is conclusive evidence at law and in equity, as against the Crown and all other persons, that the person named in the title as registered owner is indefeasibly entitled to an estate in fee simple to the land described in the indefeasible title, subject to the following:
>
> > (a) the subsisting conditions, provisos, restrictions, exceptions and reservations, including royalties, contained in the original grant or contained in any other grant or disposition from the Crown;
> >
> > (b) a federal or Provincial tax, rate or assessment at the date of the application for registration imposed or made a lien or that may after that date be imposed or made a lien on the land;
> >
> > (c) a municipal charge, rate or assessment at the date of the application for registration imposed or that may after that date be imposed on the land, or which had before that date been imposed for local improvements or otherwise and that was not then due and payable, including a charge, rate or assessment imposed by a public body having taxing powers over an area in which the land is located;

> (d) a lease or agreement for lease for a term not exceeding 3 years if there is actual occupation under the lease or agreement;
>
> (e) a highway or public right of way, watercourse, right of water or other public easement;
>
> (f) a right of expropriation or to an escheat under an Act;
>
> (g) a caution, caveat, charge, claim of builder's lien, condition, entry, exception, judgment, notice, pending court proceeding, reservation, right of entry, transfer or other matter noted or endorsed on the title or that may be noted or endorsed after the date of the registration of the title;
>
> (h) the right of a person to show that all or a portion of the land is, by wrong description of boundaries or parcels, improperly included in the title;
>
> (i) the right of a person deprived of land to show fraud, including forgery, in which the registered owner has participated in any degree;
>
> (j) a restrictive condition, right of reverter, or obligation imposed on the land by the Forest Act, that is endorsed on the title.

[406] In my view, s. 23 of the *LTA* does not assist the defendants in these proceedings.

[407] The law is well settled that the *LTA* does not oust the jurisdiction of a court of equity to grant a remedy against a person found to be subject to an equitable obligation, including one based on unjust enrichment. In *Tolley v. Guerin*, [1926] S.C.R. 566, the Supreme Court held that the provisions of a Land Title Act employing a Torrens System of title do not oust the equitable jurisdiction of the Court (see also *Bainville v. White*, 2002 BCCA 239).

[408] In these proceedings, the claim against the registered owners of the subdivided lots is based on allegations that they either committed a wrongful act, are legally responsible for the wrongful acts of Jaswant and his companies, or have been unjustly enriched at the expense of the plaintiffs. None of these claims are affected by the existence of a registered interest.

[409] In *Ng v. Ng,* 2012 BCCA 195, the case relied upon by Wills and Dale, the Court of Appeal upheld the decision of the trial judge, Justice Cullen, that a certain property was not held in trust by the plaintiff for one of the defendants who had

counter-claimed for that relief. I can see no support in that decision for the proposition that an equitable claim against a registered owner of property is defeated by registration of the defendant's title to the property in issue in the Land Title Office. I also note that at para. 29 of *Ng,* the Court referred to a number of authorities in which equitable relief had been granted against a defendant who had registered title to the land in dispute.

[410] In this case any remedy I have granted against the defendants has been based on establishing a cause of action against them. The fact that they have a registered interest in the Project lands does not prevent them from being answerable for their conduct. Section 23 of the *LTA* protects the title acquired by persons in accordance with its provisions. It does not provide any defence to an action against persons who have acquired property in circumstances in which they are required to account for it.

[411] I therefore find that s. 23 of the *LTA* does not assist the defendants.

The Garchas' Other Claims

Unjust enrichment

[412] Because I am satisfied that my findings on breach of trust and breach of fiduciary duty are sufficient to grant appropriate relief to the Garchas, I do not find it necessary to deal with their claims for unjust enrichment.

[413] The essence of the Garchas' claim is to follow their own property into the proceeds of sale of the subdivided lots. I have found that they have established that claim. They therefore are not required to establish the elements of unjust enrichment to be entitled to relief.

Conspiracy

[414] In the course of final submissions, counsel for the Garchas abandoned this claim.

Punitive damages

[415] The Garchas seek an award of punitive damages in the amount of $500,000 against all defendants except the Trustee. However, they did not address the requirements for such an award set out by the Supreme Court in *Whiten v. Pilot Insurance Co.*, 2002 SCC 18, and *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 SCC 19.

[416] In those cases, the Supreme Court of Canada held that an award of punitive damages should be restricted to cases in which the defendant's conduct represents a marked departure from ordinary standards of human behaviour. In addition, there must be a rational basis for the award of punitive damages, and that basis will only exist if a compensatory award is insufficient to serve the purposes of denunciation and deterrence. In para. 87 of *Performance Industries*, Justice Binnie stated the principle as follows:

> 87 O'Connor's fraud was, of course, reprehensible. Indeed, fraud is generally reprehensible, but only in exceptional cases does it attract punitive damages. In this case, the trial judge, at para. 109, thought punishment above and beyond the payment of generous compensatory damages was required for two reasons, namely that O'Connor's actions (1) "demand an award which will stand as an example to others" and (2) "at the same time assure that O'Connor does not unduly profit from his conduct." These are both legitimate objectives for the award of punitive damages (*Whiten*, supra, at paras. 43, 111). However, it must be kept in mind that an award of punitive damages is rational "if, but only if" compensatory damages do not adequately achieve the objectives of retribution, deterrence and denunciation.

[417] In this case Jaswant and 690174 are the only defendants whose conduct may be said to have constituted a marked departure from ordinary standards of human behaviour. However, the award I have made against them requires them to disgorge any benefit they obtained from their wrongful conduct regardless of any actual loss suffered by the Garchas. I conclude that this award adequately achieves the objectives set out by Justice Binnie.

[418] The claim for punitive damages is accordingly dismissed.

The Grewal Parties' Claims

[419] Each of the Grewal plaintiffs alleges that he, or his wholly owned company on his behalf, entered into an oral agreement with Jaswant to participate in the Project on terms that differed significantly from any of the written agreements put into evidence.

[420] In addition, each alleges that the agreements they made with Jaswant are binding on the members in the 2011 Joint Venture and that they compel the members of the 2011 Joint Venture to share the profits of the Project with them based on the amount that each participant in the Project contributed to the capital necessary to carry it out.

[421] There is however an important difference between Grewal Management's claim and the claims of Mr. Mattu and Rajpreet. Grewal Management entered into a written agreement purporting to govern the terms on which it invested in the Project. Neither Rajpreet nor Mr. Mattu entered into a written agreement with respect to their investments.

Grewal Management's claim

[422] I have set out my findings with respect to Grewal Management becoming involved in the Project at paras. 104-117 of these reasons.

[423] Grewal Management's position is that it invested in the Project pursuant to the oral agreement I described in those paragraphs and that the oral agreement supersedes the written agreement set out in the 2011 JVA.

[424] Mr. Grewal testified that he and Jaswant agreed that there would be an accounting when the Project was completed with all lots sold and expenses paid that would calculate how the profits would be divided based on relative contributions to the Project. While Mr. Grewal did not expressly say so, it is clear that when he referred to contributions, he meant monetary contributions.

[425] The defendants' position is that the whole of the net profits from the Project should be divided in accordance with the proportionate shares of each of the 2011

Joint Venturers. This would result in Grewal Management being entitled to 14.25% of the net profits.

[426] The actual contribution to Project expenses made by Grewal Management is not in dispute. In June 2011, Grewal Management contributed $1,687,886.50 to Buckley Hogan to be used to pay part of the purchase price for Lot 5. On March 19, 2012, it received $740,498.38 from the proceeds of the WSCU mortgage that paid out the Acquisition Mortgages on Lots 1 to 5. As in the case of the other 2011 Joint Venturers, I regard this receipt as an advance distribution of proceeds from the Project.

[427] The issue is whether the agreement pursuant to which Grewal Management participated in the Project was wholly reduced to writing or whether the oral agreement alleged by Mr. Grewal supersedes or modifies the written agreement set out in the 2011 JVA.

[428] I have concluded that Grewal Management is bound by the terms of the 2011 JVA, which explicitly set out the proportionate interest of each 2011 Joint Venturer in the Project.

[429] An oral agreement can in some circumstances constitute a collateral agreement that explains or expands upon a written agreement. However, an oral agreement that contradicts the express terms of a written agreement is of no effect: Fridman at 517.

[430] The oral agreement alleged by Grewal Management contradicts the written agreement it executed. It is therefore of no effect and Grewal Management is bound by the terms of the written agreement it executed pursuant to the parol evidence rule.

[431] The parol evidence rule was succinctly described in *Sattva*:

> 59 It is necessary to say a word about consideration of the surrounding circumstances and the parol evidence rule. The parol evidence rule precludes admission of evidence outside the words of the written contract that would add to, subtract from, vary, or contradict a contract that has been wholly reduced to writing (*King*, at para. 35; and Hall, at p. 53). To this end, the rule

> precludes, among other things, evidence of the subjective intentions of the parties (Hall, at pp. 64-65; and *Eli Lilly & Co. v. Novopharm Ltd.*, [1998] 2 S.C.R. 129 (S.C.C.), at paras. 54-59, per Iacobucci J.). The purpose of the parol evidence rule is primarily to achieve finality and certainty in contractual obligations, and secondarily to hamper a party's ability to use fabricated or unreliable evidence to attack a written contract (*C.J.A., Local 579 v. Bradco Construction Ltd.*, [1993] 2 S.C.R. 316 (S.C.C.), at pp. 341-42, per Sopinka J.).

[432] In addition, in this case the entire agreement clause in the November 2010 JVA expressly stated that the written agreement superseded all agreements with respect to the Project. While Mr. Grewal did not read the November 2010 JVA, the 2011 JVA expressly incorporated its terms by reference and Grewal Management must be taken to have agreed to be bound by it, including the entire agreement clause found at para. 13.1.

[433] A further difficulty I have with Mr. Grewal's submission is that it does not satisfactorily explain why he executed the 2011 JVA within days after the alleged oral agreement. There is no evidence that Mr. Grewal communicated any concern about Grewal Management's rights as set out in the 2011 JVA to anyone at the time it was executed.

[434] I find that the terms of the 2011 JVA were clear and capable of only one reasonable interpretation: that the profits from the 2011 Joint Venture would be distributed in accordance with the agreed proportionate interests set out in that agreement. I am reinforced in my interpretation by the fact that the sole purpose of the 2011 JVA was to admit Grewal Management into the joint venture and to adjust the proportionate interests of the parties accordingly.

[435] I therefore conclude that Grewal Management is bound by the terms of the 2011 JVA, which limit it to receiving 14.25% of the net proceeds of the Project.

Jaswant's fiduciary duties to Grewal Management

[436] Mr. Grewal's position is that Jaswant owed a fiduciary duty to Grewal Management with respect to the Project. His counsel submitted that this fiduciary duty arose from the *de facto* control that Jaswant exercised over all aspects of the

Project and from the representations that Jaswant made with respect to how the proceeds of the Project would be divided.

[437] I am not satisfied that Jaswant owed a fiduciary duty to Grewal Management or Mr. Grewal with respect to the negotiation of the terms on which Grewal Management became a member of the 2011 JVA or invested in the Project. As I have indicated above in the discussion of *Zynik Capital Corp.*, parties who are merely negotiating the terms of a joint venture do not generally owe fiduciary duties to one another.

[438] I am satisfied that Jaswant owed a fiduciary duty to Grewal Management with respect to the affairs of the 2011 Joint Venture. However, I do not find that Jaswant breached those fiduciary duties. All of the funds he invested were used in the Project. Mr. Grewal was involved in the negotiation of the Virk Mortgage, the Land Swap, and the subdivision of the Project. Jaswant carried out those steps with the informed consent of the 2011 Joint Venturers including Grewal Management, all of whom benefitted from them.

Rajpreet Sangha's claim

[439] I have already made a finding that Rajpreet advanced $800,000 to Panorama and Jaswant in connection with the Project. The first $200,000 was initially advanced as a contribution to the October 2010 Joint Venture by 0892995. Panorama owed a fiduciary duty to 0892995 to use that advance solely for the purposes of the October 2010 Joint Venture. Because that joint venture did not proceed, the $200,000 should have been kept segregated and returned to 0892995. However, Panorama used those funds to make up part of the deposit for the purchase of Lot 5. 0892995 therefore had a right to trace those funds into Lot 5 and ultimately Panorama's interest in the 2011 Joint Venture.

[440] I also find that the subsequent agreement made between Rajpreet, Jaswant, and their respective companies had all of the essential elements of a joint venture, set out at para. 231 of these reasons. Rajpreet agreed to combine his contributions with those of others into the Project. There is no suggestion that any of the funds

advanced by Rajpreet or 0892995 were advanced as loans. I find that they were advanced as contributions to a joint venture, the object of which was to acquire and subdivide Lots 1 to 5 and sell those lots; in other words, the Project. I also find that this joint venture agreement contained a formula for determining each party's share of the proceeds.

[441] I therefore conclude that the agreement made between Jaswant and Rajpreet in 2010, pursuant to which Rajpreet made his investment, was a joint venture agreement pursuant to which Rajpreet obtained a beneficial ownership interest in the Project.

[442] The agreement between Rajpreet and Jaswant was made after the execution of the November 2010 JVA, which purported to fully allocate the ownership of the Project. The question this raises is the extent to which the interests of any November 2010 Joint Venturer, apart from Jaswant and the two companies he wholly owned and controlled, could be affected by the agreement between Rajpreet and Jaswant.

[443] All of the members of the November 2010 Joint Venture testified that they never authorized Jaswant to bind them to make any agreements altering their rights under that agreement. They also rely on the terms of the November 2010 JVA that limit the authority of any joint venture to bind the others.

[444] There are circumstances in which a person may be bound by an agreement made by another person. This most commonly arises in an agency relationship.

[445] A person may bind another if they have actual authority or ostensible authority to do so.

[446] Ostensible authority requires some communication from the principal to the third party that would cause the third party reasonably to believe that the agent had authority to bind the principal. In this case I cannot find sufficient evidence that the November 2010 Joint Venturers held out Jaswant as their agent in his dealings with Rajpreet to establish ostensible authority. There is virtually no evidence of any

communications between Rajpreet and the November 2010 Joint Venturers or that Rajpreet was even aware of the November 2010 Joint Venture.

[447] For Rajpreet to affect the rights of the other November 2010 Joint Venturers he must therefore establish that Jaswant had actual authority to bind them.

[448] The existence of actual authority is a question of fact that must be determined on a review of the evidence. The principles relating to a finding of actual authority were set out in *Grosvenor Canada Limited v. South Coast British Columbia Transportation Authority*, 2015 BCSC 177:

> 58 The parties agree the essential elements of an agency relationship are (a) the principal's control of the agent's action, (b) the consent of both the agent and the principal, and (c) the authority of the agent to affect the principal's legal position. Professor Fridman in *Canadian Agency Law* 2nd Ed. (Toronto: LexisNexis Canada Inc., 2012) defines agency at common law as follows (at p. 4):
>
> > Agency is a relationship that exists between two persons when one, called the agent, is considered in law to represent the other, called the principal, in such a way as to be able to the affect the principal's legal position in respect of strangers to the relationship by the making of contracts or the disposition of property.
>
> 59 The existence of an agency relationship is a question of fact and it may arise between parties who have another legal relationship. In the context of trustees acting as agents, see *Advanced Glazing v. Multimetro et al.*, 2000 BCSC 804. It is irrelevant that the parties have used the term agency in describing their relationship (Fridman, *Canadian Agency Law* at p. 6). No express agreement is necessary to establish an agency relationship, and therefore it can be implied from the circumstances: *Trident Holdings Ltd. v. Danand Investments Ltd.* (1988), 64 O.R. (2d) 65 (C.A.).

[449] I have no difficulty in finding that Jaswant had actual authority to bind his companies, 690174 and Panorama. He was their directing mind and was acting on their behalf in the Project. I have already found that he had actual authority to bind Parmjit and that they were in fact engaged in a joint enterprise with respect to the Project. I also have found that Wills and Dale held their interest in the November 2010 Joint Venture as nominees for Jaswant, and that he therefore had the authority to deal with their interests in the Project to complete it successfully.

[450] The totality of the circumstances under which the Project was formed and pursued have convinced me that Jaswant had the actual authority to take the steps necessary to complete the Project, including by bringing in additional investors to provide funds to meet the expenses necessary to bring it to fruition.

[451] The evidence shows that in fact Jaswant made almost all of the decisions with respect to the Project without consulting with the other members of the November 2010 Joint Venture. There is no evidence of any November 2010 Joint Venturer ever challenging any decision Jaswant made. Remarkably, there is no evidence of any negotiations about the proportionate interests of the parties to the November 2010 JVA. On the contrary, it appears that Jaswant unilaterally decided what those interests would be.

[452] There is also no evidence that any of the November 2010 Joint Venturers except Ranjit played any role in the acquisition of Lots 2 to 4. Ranjit was involved in the acquisition of Lot 2, but his evidence was that he was not aware that Lot 2 was going to be consolidated and subdivided when he purchased a half interest in it. His belief was that Lot 2 was to be held for investment purposes. Although he signed the November 2010 JVA, there is no evidence that Ranjit participated in its negotiation or in the determination of the proportionate interests of the November 2010 Joint Ventures. Wills and Dale played no role in the acquisition of Lot 4 apart from executing the Lot 4 Acquisition Mortgage, and neither Mr. Wills nor Ms. Dale knew what they would receive from the completed Project.

[453] I find that Jaswant had the actual authority of the members of the November 2010 Joint Venture to do what was necessary to raise the funds required to complete the Project, including the agreement he made with Rajpreet.

[454] Because Rajpreet was not a party to the November 2010 JVA and was not aware of it, he is not bound by any of the contractual provisions in it restricting collateral agreements.

[455] The result is that Rajpreet has established a joint venture agreement with Jaswant that must be taken into account in determining the distribution of the proceeds of the Project.

Daljit Singh Mattu's claim

[456] Mr. Mattu invested $1,062,041.45 in the Project. As with Rajpreet, the critical issue with relation to his claim is how this amount should be characterized.

[457] Jaswant agrees that he borrowed $400,000 from Mr. Mattu and used those funds to invest in Sangha Group 2. The documentary evidence indicates that from November 2006 to February 2007, Mr. Mattu advanced approximately $400,000 to Jaswant, which he used to fund land acquisitions for Sangha Group 2.

[458] As I have earlier stated, Jaswant agrees that those funds were advanced as a loan and that he agreed to repay $500,000 to Mr. Mattu once Sangha Group 2 was completed.

[459] When Mr. Mattu inquired about the $500,000.00 repayment in 2007, Jaswant told him he needed to wait a little longer to be paid. In October 2007, after Mr. Mattu again asked for the repayment, Jaswant told him about the Project and gave him the option of taking the $500,000.00 repayment or investing it in the Project. Mr. Mattu visited the site and decided to invest.

[460] Mr. Mattu testified that Jaswant told him that the subdivision was his and that more properties would be acquired. He denies having knowledge of the involvement of other parties at that time.

[461] Jaswant acknowledged that he agreed the $500,000.00 due to Mr. Mattu would be invested in the Project, and that he invested the $500,000.00 in the Project on Mr. Mattu's behalf. However, as I described earlier in these reasons, his position is that he used the funds because Mr. Mattu was his silent partner in all his business activities. I need not repeat my reasons for rejecting that evidence.

[462] I have also accepted Mr. Mattu's evidence that most of his further advances to Jaswant were made pursuant to the same agreement. The bulk of Mr. Mattu's

advances to Jaswant were made in 2007 and 2008, the period during which Lots 2 to 4 were being acquired.

[463] I find that the agreement between Jaswant and Mr. Mattu has all of the necessary characteristics of a joint venture.

[464] Mr. Mattu did not use the term joint venture in his evidence. However, I find his agreement was summarized accurately in his counsel's argument:

> a. funds Mr. Mattu advanced to Mr. Sangha or his companies would be used by Mr. Sangha only to acquire properties for the Project or to pay costs associated with the Project;
>
> b. Mr. Sangha would involve other investors, and keep records to keep track of amounts advanced by other investors;
>
> c. Mr. Sangha would keep records of all of the bills for the Project, which investors could access;
>
> d. Mr. Sangha would be "in charge" of the Project and hire people for the Project;
>
> e. after the Project was complete and lots sold, and all costs and any legitimate creditors directly associated with the Project, including bank and contractors, had been paid, the remaining proceeds would be divided proportionately among investors according to their proven investments in the Project.

[465] Arguably the only element of a joint venture lacking in this description, as set out in *Gettling,* is a right of mutual control. It is clear that Jaswant exercised a great deal of control over the Project. However, this does not mean that Mr. Mattu had no right to control aspects of the Project.

[466] Mr. Mattu was clearly actively involved in the financial management of the Project from 2010 onwards. He introduced Rajpreet and later Jasprit Grewal to Jaswant. He raised funds needed to move the Project forward. He provided security for the Virk Mortgage, which was necessary for the Project to proceed. He clearly had control over all of these activities.

[467] Surrounding circumstances also support the conclusion that there was a joint venture between Jaswant and Mr. Mattu with respect to the Project:

1. Jaswant had historically structured projects relating to land developments in which investors were involved as joint ventures.

2. Jaswant adopted a joint venture structure to arrange for the involvement of the participants in the 2007, October 2010, November 2010, and 2011 JVAs.

3. All of the written joint venture agreements provided that the joint venturers owned a share of the joint venture assets as their separate property.

[468] I therefore find that Mr. Mattu entered into a joint venture with Jaswant pursuant to which Mr. Mattu acquired a beneficial interest in the Project by providing funds and assisting in its completion. The only rational basis for Mr. Mattu providing security for the Virk Mortgage was to carry out the objectives of the Project. He had no reason to put his property at risk unless he was a participant in the Project.

[469] I find that Mr. Mattu must have been aware of the existence of the November 2010 JVA by no later than June 2011. He introduced Mr. Grewal to the Project. Mr. Mattu witnessed the signatures of many of the 2011 Joint Venturers to the 2011 JVA. Even if he did so before some of the 2011 Joint Venturers had executed it, he must have been aware of the 2011 JVA by then. There is no evidence that Mr. Mattu communicated any objection to the terms of the November 2010 or 2011 JVAs at that time. This however is also consistent with him being a participant in Jaswant's interest in the Project.

[470] As set out above, there is ample evidence that Mr. Mattu was involved in the management of the Project, particularly with respect to finding investors and assisting in executing documentation. The only question is whether Mr. Mattu was participating in the Project because he was Jaswant's partner in all of the business activities carried out by Jaswant and his companies, or whether his activities and investment were restricted to the Project. I repeat my finding that Mr. Mattu was not a participant in any of Jaswant's business activities apart from the Project. I find that he became an investor in the Project in 2007 when Jaswant invested $500,000 from Sangha Group 2 on his behalf into the Project and that from that time forward was

engaged in the joint venture that developed the Project. I am satisfied that the funds he advanced, either directly or through his agreement with respect to the $500,000 from Sangha Group 2, were investments in the capital required to complete the Project.

[471] I also find that the November 2010 and 2011 Joint Venturers became aware of his involvement in the Project by 2011 at the latest.

[472] The memorandum prepared by Sean Hogan, which I described at paras. 126-128, supports the conclusion that the 2011 Joint Venturers were aware of Mr. Mattu's investment and recognized that he was a participant in the Project. They must have been aware of the reasons for Mr. Mattu's involvement in obtaining the Virk Mortgage. I also consider it significant that it was Ranjit and Mr. Grewal who first described Mr. Mattu as a silent partner and instructed Buckley Hogan to include him in the mortgage of the phase 1 lots. It is clear to me that their reference to Mr. Mattu being a silent partner referred to his interest in the Project. From this I conclude that they were aware of his involvement and did not object to it. This reinforces my conclusion that the 2011 Joint Venturers were aware that Mr. Mattu would share in the revenue from the Project.

Jaswant owed a fiduciary duty to Mr. Mattu and Rajpreet

[473] It is trite to say that both contractual and fiduciary duties can arise out of the same relationship. I am of the view that Jaswant obtained the use of Mr. Mattu's and Rajpreet's funds in circumstances which imposed an *ad hoc* fiduciary duty on him to use them for the specific purposes of securing them an interest in the Project.

[474] The existence of an *ad hoc* fiduciary duty is dependent on the specific circumstances of a relationship. The circumstances giving rise to an *ad hoc* fiduciary duty were reviewed in *Elder Advocates of Alberta Society v. Alberta*, 2011 SCC 24:

> 30 First, the evidence must show that the alleged fiduciary gave an undertaking of responsibility to act in the best interests of a beneficiary: *Galambos*, at paras. 66, 71 and 77-78; and Hodgkinson, per La Forest J., at pp. 409-10. As Cromwell J. wrote in *Galambos*, at para. 75: "what is required in all cases is an undertaking by the fiduciary, express or implied, to act in accordance with the duty of loyalty reposed on him or her."

> 31 The existence and character of the undertaking is informed by the norms relating to the particular relationship: *Galambos*, at para. 77. The party asserting the duty must be able to point to a forsaking by the alleged fiduciary of the interests of all others in favour of those of the beneficiary, in relation to the specific legal interest at stake.
>
> 32 The undertaking may be found in the relationship between the parties, in an imposition of responsibility by statute, or under an express agreement to act as trustee of the beneficiary's interests. . . .
>
> 33 Second, the duty must be owed to a defined person or class of persons who must be vulnerable to the fiduciary in the sense that the fiduciary has a discretionary power over them. Fiduciary duties do not exist at large; they are confined to specific relationships between particular parties. Per se, historically recognized, fiduciary relationships exist as a matter of course within the traditional categories of trustee-cestui qui trust, executor-beneficiary, solicitor-client, agent-principal, director-corporation and guardian-ward or parent-child. By contrast, ad hoc fiduciary relationships must be established on a case-by-case basis.
>
> 34 Finally, to establish a fiduciary duty, the claimant must show that the alleged fiduciary's power may affect the legal or substantial practical interests of the beneficiary: *Frame*, per Wilson J., at p. 142.
>
> [Emphasis added]

[475] I do not understand the reference in *Elder Advocates* to a requirement that the alleged fiduciary act exclusively in the interest of the beneficiary to preclude finding a fiduciary duty to act in the mutual interests of the fiduciary and beneficiary. This situation will often arise when, as in this case, the parties are jointly pursuing a business opportunity, such as a joint venture.

[476] The circumstances of Mr. Mattu’s and Rajpreet’s investments in the Project that gave rise to an *ad hoc* fiduciary duty with respect to their investments were as follows:

1. Jaswant had undertaken to use the funds contributed by them for the purposes of completing the Project.

2. Jaswant had control of the funds invested by them and discretion as to how to use them.

3. The manner in which Jaswant used the funds clearly could affect their legal and practical interest in the Project.

4. The only recourse that they had to recover their investment was to obtain a share of the net proceeds of the Project.

[477] With respect to the “vulnerability” requirement, it is important to note that vulnerability must be assessed after the relationship in question has been entered into. This principle was addressed by Justice Cromwell in *Galambos v. Perez*, 2009 SCC 48:

> 68 . . . fiduciary law is more concerned with the position of the parties that results from the relationship which gives rise to the fiduciary duty than with the respective positions of the parties before they enter into the relationship. La Forest J. in *Hodgkinson*, at p. 406, made this clear by approving these words of Professor Ernest J. Weinrib: "It cannot be the *sine qua non* of a fiduciary obligation that the parties have disparate bargaining strength. . . . In contrast to notions of conscionability, the fiduciary relation looks to the relative position of the parties that results from the agreement rather than the relative position that precedes the agreement" ("The Fiduciary Obligation" (1975), 25 U.T.L.J. 1, at p. 6). Thus, while vulnerability in the broad sense resulting from factors external to the relationship is a relevant consideration, a more important one is the extent to which vulnerability arises from the relationship: *Hodgkinson*, at p. 406.

[478] I am therefore satisfied that Rajpreet and Mr. Mattu became vulnerable to Jaswant when they provided him with their investments in the Project, and that all of the elements necessary to establish an *ad hoc* fiduciary duty were present.

Are Rajpreet and Mr. Mattu entitled to a constructive trust over the proceeds of lot sales?

[479] A critical issue with respect to Rajpreet’s and Mr. Mattu’s claims is whether they are entitled to a constructive trust over the subdivided lots, and if so, when the trust took effect.

[480] A constructive trust may be imposed if the alleged trustee has engaged in wrongful conduct or has been unjustly enriched.

[481] The leading case on the circumstances necessary to impose a remedial constructive trust for wrongful conduct is *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217. In *Re Redstone Investment Corp.* 2015 ONSC 533, Justice Morawetz, as he then was, summarized the test set out in *Soulos*:

> 68 The test for finding a constructive trust based on wrongful conduct was set out by the Supreme Court of Canada in *Soulos v. Korkontzilas*, [1997] 2 S.C.R. 217 (S.C.C.). The following criteria is to be considered in determining the availability of the remedial constructive trust:
>
> > 1. The defendant must have been under an equitable obligation, that is, an obligation of the type that courts of equity have enforced, in relation to the activities giving rise to the assets in his hands;
> >
> > 2. The assets in the hands of the defendant must be shown to have resulted from deemed or actual agency activities of the defendant in breach of his equitable obligation to the plaintiff;
> >
> > 3. The plaintiff must show a legitimate reason for seeking a proprietary remedy, either personal or related to the need to ensure that others like the defendant remain faithful to their duties; and
> >
> > 4. There must be no factors which would render imposition of a constructive trust unjust in all the circumstances of the case; e.g., the interests of intervening creditors must be protected.

[482] I adopt this analysis of *Soulos*. However, subsequent to *Redstone* the Supreme Court has held that the equitable obligation referred to in the preceding passage need not be of a fiduciary nature, and that a breach of any obligation that a Court would enforce may be sufficient: *Moore v. Sweet*, 2018 SCC 52.

[483] A constructive trust may also be imposed against a party pursuant to the equitable doctrine of unjust enrichment if, as per *Garland v. Consumers' Gas Co.,* 2004 SCC 25 at para. 30, there exists:

1. An enrichment of that party;

2. A corresponding deprivation of the plaintiff; and

3. An absence of a juristic reason for the enrichment.

[484] In this case I am satisfied that Rajpreet and Mr. Mattu are entitled to the remedy of a constructive trust on both of the above grounds.

A constructive trust is available based on wrongful conduct

[485] I find that the elements necessary to establish a constructive trust against the interests of the Bankrupts and Parmjit in the Project are present in this case. All of these defendants knew that Rajpreet and Mr. Mattu had invested in the Project

based on Jaswant's agreement that they would participate in it. I have included Parmjit in this category because of my finding that she and Jaswant were engaged in a joint enterprise in pursuing the Project. I am satisfied that by obtaining Rajpreet's and Mr. Mattu's investments on the basis that they would be participants in the Project, Jaswant was under an obligation to them that a Court of Equity would have enforced. The defendants referred to in this paragraph knew and profited from Jaswant's breach of that obligation. For the reasons I have set and out in paras. 562-568 below I find that the constructive trust came into existence prior to the Bankruptcies.

[486] On the facts I have found Jaswant and Parmjit could not in good conscience have retained the benefit of Rajpreet's and Mr. Mattu's investments without ensuring that they participated in the Project. The good conscience basis for imposing a constructive trust was expressly approved in *Soulos*:

> 29 Good conscience as the unifying concept underlying constructive trust has attracted the support of many jurists. Edmund Davies L.J. suggested that the concept of a "want of probity" in the person upon whom the constructive trust is imposed provides "a useful touchstone in considering circumstances said to give rise to constructive trusts": *Carl Zeiss Stiftung v. Herbert Smith & Co. (No. 2)*, [1969] 2 Ch. 276 (C.A.), at p. 301. Cardozo J. similarly endorsed the unifying theme of good conscience in *Beatty v. Guggenheim Exploration Co.*, 122 N.E. 378 (1919), at p. 380:
>
> > A constructive trust is the formula through which the conscience of equity finds expression. When property has been acquired in such circumstances that the holder of the legal title may not in good conscience retain the beneficial interest, equity converts him into a trustee.

[487] I repeat that the contributions of Rajpreet and Mr. Mattu made a material contribution to the acquisition of Lots 2 to 4 and to the payment of Project expenses.

[488] I also find that there is a legitimate reason for these plaintiffs to seek a proprietary remedy in this case. The obtaining of a proprietary interest in the subdivided lots is the only effective remedy available to them. Given the insolvency of the bankrupt defendants, a personal remedy would clearly be inadequate.

[489] Finally, there is no other factor that would make the imposition of a proprietary remedy unjust in the circumstances. While the Trustee maintains that a constructive

trust should not be imposed to the prejudice of the creditors of the bankrupt estates, I find that it would be unjust for the creditors to obtain the benefit of the plaintiffs' investment in the circumstances I have outlined above.

[490] As pointed out by Justice Morawetz in *Redstone,* the interests of the general body of creditors in a bankruptcy is not a factor that will render the imposition of a constructive trust unjust if the property over which the trust is imposed would not have been available to the creditors without the wrongful acts of the insolvent defendant. In such a case it would be unjust to permit the general body of creditors to benefit from the wrongful acts of that defendant.

A constructive trust is available based on unjust enrichment

[491] If I am wrong in finding that Jaswant owed a fiduciary duty with respect to Rajpreet and Mr. Mattu, he nevertheless had a contractual obligation to ensure their participation in the Project. This raises the question of whether a breach of that contractual obligation is sufficient to warrant the imposition of a constructive trust in their favour based on unjust enrichment.

[492] The traditional view was that in order to establish a claim in unjust enrichment against an innocent third party the claimant must show a breach of an equitable duty on the part of the wrongdoer. However, in *Moore*, the majority imposed a constructive trust which arose from the deprivation of a contractual right. Justice Coté stated this principle as follows:

> 49 My view is that it is not useful, in the context of unjust enrichment, to distinguish between expectations based on a contractual obligation and expectations where there was a breach of an equitable duty (see my colleagues' reasons, at para. 104). Rather, a robust approach to the corresponding deprivation element focuses simply on what the plaintiff actually lost — that is, property that was in his or her possession or that would have accrued for his or her benefit — and on whether that loss corresponds to the defendant's enrichment, such that we can say that the latter was enriched *at the expense* of the former. As was observed by Professors Maddaugh and McCamus in *The Law of Restitution*, one source of difficulty in these kinds of disappointed beneficiary cases is
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> > a rigid application of the "corresponding deprivation" or "expense" element as if it requires that the benefit in the defendant's hands must have been transferred from, or constitute an out-of-pocket expense of, the plaintiff. . . .

> > [R]estitution of benefits received from third parties may well provide a basis for recovery. In this particular context, the benefit received can, in any event, normally be described as having been received at the plaintiff's expense in the sense that, but for the mistaken failure to implement the arrangements in question, the benefit would have been received by the plaintiff. [Emphasis added; p. 35-21.]
>
> I agree. In this case, given the fact that Michelle held up her end of the bargain, kept the policy alive by paying the premiums, did not predecease Lawrence, and still did not get what she actually contracted for, it seems artificial to suggest that her loss was anything less than the right to receive the entirety of the insurance proceeds.

[493] The facts of *Moore* were different from those of these proceedings. However, the legal analysis of the majority decision is in my view applicable to the facts before me.

[494] The claimant in *Moore* was the first wife of a deceased person who had been named as sole beneficiary in the deceased's life insurance policy. The premiums on the policy were initially paid from the couple's joint account. When the marriage broke down, the applicant and the deceased made an oral agreement that the applicant would pay the premiums from her own funds and would continue to be the designated beneficiary of the policy. Thereafter, the claimant made all of the premium payments.

[495] After divorce, the deceased entered into a relationship with the respondent. At some later date he revoked the claimant's designation as beneficiary and instead designated the respondent as an irrevocable beneficiary as permitted by the applicable Ontario insurance legislation. When the deceased died, the claimant was denied payment under the policy. She then brought proceedings for an order that she was entitled to the death benefit. She succeeded at first instance, but that decision was reversed by the Ontario Court of Appeal.

[496] The Supreme Court of Canada reversed the Court of Appeal and held that the applicant was entitled to the death benefit. Notwithstanding the fact that her claim was based on a breach of contract, the majority of the Court found that the applicant was entitled to a constructive trust over the proceeds of the policy based on unjust enrichment. In so doing, the Court found that the applicant had been unjustly

deprived of the whole of the death benefit and not just the premiums she had paid on the policy.

[497] Justice Coté emphasized that the underlying principle of unjust enrichment was the notion of restoration of a benefit which justice did not permit another person to retain:

> 38 This principled approach to unjust enrichment is a flexible one that allows courts to identify circumstances where justice and fairness require one party to restore a benefit to another. Recovery is therefore not restricted to cases that fit within the categories under which the retention of a conferred benefit was traditionally considered unjust (*Kerr*, at para. 32). As observed by McLachlin J. in *Peel (Regional Municipality)* (at p. 788):
>
> > The tri-partite principle of general application which this Court has recognized as the basis of the cause of action for unjust enrichment is thus seen to have grown out of the traditional categories of recovery. It is informed by them. It is capable, however, of going beyond them, allowing the law to develop in a flexible way as required to meet changing perceptions of justice.

[498] In *Moore*, the Court also reiterated the two-step analysis of the issue of whether there was a juristic reason for the deprivation and enrichment. The analysis places the initial onus on the plaintiff to show that the established categories of juristic reasons (such as contract, statutory provision, or gift) do not apply. Once the plaintiff establishes that those categories do not apply the onus shifts to the defendant to establish a juristic reason for the enrichment.

[499] Justice Coté held that a claimant is not required to prove that the benefit was bestowed directly on the defendant, and that the amount of the deprivation can be based on the amount of a gain of which the claimant had been deprived. Thus, the claimant was entitled to receive the whole of the death benefit and not just the amount she paid in premiums.

[500] In this case, Jaspreet and Mr. Mattu have clearly been deprived of a benefit: the right to share in the profits of the Project. The 2011 Joint Venturers have collectively received a corresponding benefit.

[501] However, Rajpreet, Parmjit, and Wills and Dale submit that they are *bona fide* purchasers for value of their interests in the November 2010 and 2011 Joint

Ventures without notice of the claims of Mr. Mattu and Rajpreet, and that this is a juristic reason for their enrichment.

[502] I have concluded that this defence is not available to the defendants. I have already found that Parmjit was content to let Jaswant act on her behalf in the Project. In my view the finding that Parmjit and Jaswant were engaged in a joint enterprise makes Parmjit responsible for Jaswant's wrongful acts with respect to Rajpreet and Mr. Mattu.

[503] I also am satisfied that Ranjit was aware of Mr. Mattu's involvement in the Project from an early point in its development and that Ranjit was, at the very least, in possession of sufficient facts to put him on inquiry with respect to Mr. Mattu's involvement. It follows from the concession made by counsel that Svender is also to be taken to have had notice of Mr. Mattu's interest in the Project.

[504] I have already concluded that Wills and Dale hold their interest in the Project as nominees for Jaswant. Given this fact, they are not *bona fide* purchasers for value with respect to that interest. As neither the Trustee nor any of the other members of the 2011 Joint Venture, other than Grewal Management, have sought any remedy against Wills and Dale, they continue to be entitled to share in the profits of the 2011 Joint Venture, subject to the established claims of Rajpreet and Mr. Mattu.

[505] In addition, as I have already indicated, I am satisfied that Jaswant had the actual authority to do what was necessary to finance the Project. The fact that the 2011 Joint Venturers are parties to a contract pursuant to which they are entitled to certain rights does not insulate them from a claim based on unjust enrichment. None of them contributed their proportionate share of the expenses incurred to complete the Project. Many of those expenses were paid from funds provided by Rajpreet and Mr. Mattu. There is therefore a direct link between their enrichment and Mr. Mattu's deprivation.

[506] I therefore find that the defence of being *bona fide* purchasers for value has not been made out by the 2011 Joint Venturers.

[507] With respect to the Trustee, as I have outlined elsewhere in these reasons, the funds that the Trustee says should be distributed to the creditors of the bankrupt estates would not have been available without the funds invested by Mr. Mattu and Rajpreet. Therefore, the analysis of Justice Morawetz in *Redstone* applies to the bankrupt estates.

[508] I am therefore satisfied that Rajpreet and Mr. Mattu are entitled to the remedy of a constructive trust over the net proceeds of the Project.

[509] I will quantify the extent of the constructive trust when I deal with the remedies awarded to the successful plaintiffs.

Are the Garcha, Mattu and Rajpreet Claims Equity Claims?

[510] The Trustee submits that the plaintiffs' claims in the Civil Actions are equity claims, as that term is defined in the *BIA*, and are therefore postponed to the claims of all other creditors of the Bankrupts to the funds held in the Vendor Trust Accounts set up for the Bankrupts. If this position is correct there will be nothing payable to the plaintiffs because there are insufficient assets in the bankrupt estates to pay the unsecured claims in full.

[511] The Trustee's counsel set out his position on this issue in his written submissions in the Grewal Action as follows:

> 85. Ignoring for the moment the written agreements, of importance to the classification of the Grewal Group's Equity Claims, were the allegations in their first NOCC as to the existence of a joint venture and investment agreement's terms that constituted what the Trustee viewed as a classic definition of what an Equity Claim was. An investment was alleged to contribute capital, share profit, accepting the risk of loss or profit, requiring the return of capital and a dividend or similar payment based upon a share of profit, if any. There was no allegation or suggestion by the Grewal Group that the investment monies were a loan repayable with interest or other form of debt or credit agreement.
>
> 86. The Grewal Group never once suggested in any way in evidence at trial that they were entitled to the repayment of a debt or loan or an obligation under a credit agreement.

[512] In my view the Trustee's submissions on this issue are based on the incorrect assumption that the Garchas' and Grewal plaintiffs' claims are claims to participate in the division of the property of the Bankrupts that is divisible among their creditors.

[513] This assumption is incorrect because the plaintiffs' claims are to receive their proportionate share of the profits of the joint ventures, all of which were pursuing the business of completing the Project. The property of the Bankrupts in the Project is limited to their proportionate share of the capital of the joint ventures remaining after all creditors of the Project have been paid. The proportionate shares of the non-bankrupt joint venturers are not property of the Bankrupts.

[514] The joint venturers have not made any contribution to the capital of the Bankrupts and have no right to share in the profits the Bankrupts received from the Project. The joint venturers provided capital to the joint ventures in which they participated, not to the Bankrupts. Similarly, the separate creditors of the Bankrupts have no right to claim against the proportionate shares of the non-bankrupt joint venturers.

[515] The Trustee has also failed to address the interaction between ss. 67(1) and 140.1 of the *BIA*. Section 67(1) excludes property held in trust from the property of a bankrupt divisible among its creditors. Section 140.1 applies only to the property of a bankrupt that is distributable among its creditors. The express terms of the 2007 JVA provide that 690174 held title to the assets of the 2007 Joint Venture in trust for the 2007 Joint Venturers. Apart from the 1/23 interest held by 690174, all of the property of that joint venture was beneficially owned by the 2007 Joint Venturers and is therefore not distributable among 690174's creditors.

[516] Section 140.1 provides as follows:

> **140.1** A creditor is not entitled to a dividend in respect of an equity claim until all claims that are not equity claims have been satisfied.

[517] An equity claim is defined as follows:

> *equity claim* means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,

> (b) a return of capital,
>
> (c) a redemption or retraction obligation,
>
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
>
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d); (*réclamation relative à des capitaux propres*)

[518] An equity interest is described as follows:

> *equity interest* means
>
> > (a) in the case of a corporation other than an income trust, a share in the corporation — or a warrant or option or another right to acquire a share in the corporation — other than one that is derived from a convertible debt, …

[519] Section 67(1)(a) of the *BIA* provides as follows:

> 67(1) The property of a bankrupt divisible among his creditors shall not comprise
>
> > (a) property held by the bankrupt in trust for any other person;

[520] The modern approach to statutory interpretation requires a consideration of the words of a statue in the context of the scheme of the act in which they are found; in *Re Rizzo & Rizzo Shoes Ltd.*, [1998] 1 S.C.R. 27 at 40-41:

> 21 Although much has been written about the interpretation of legislation (see, e.g., Ruth Sullivan, *Statutory Interpretation* (1997); Ruth Sullivan, *Driedger on the Construction of Statutes* (3rd ed. 1994) (hereinafter "Construction of Statutes"); Pierre-André Côté, *The Interpretation of Legislation in Canada* (2nd ed. 1991), Elmer Driedger in *Construction of Statutes* (2nd ed. 1983) best encapsulates the approach upon which I prefer to rely. He recognizes that statutory interpretation cannot be founded on the wording of the legislation alone. At p. 87 he states:
>
> > Today there is only one principle or approach, namely, the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

[521] In my view neither the ordinary meaning of the words contained in ss. 140.1 and 67(1)(a) nor the scheme of the *BIA* support the Trustee's position with respect to the Garchas' claim.

[522] The Trustee relied on a number of recent decisions that considered s. 140.1. In *Re Bul River Mineral Corp.*, 2014 BCSC 1732, Justice Fitzpatrick reviewed the law relating to the proper interpretation of s. 140.1 and decided that it had expanded the scope of claims that should be considered to be equity claims to include claims that were derived from equity holdings of the claimant. She also agreed with other cases that claims formerly considered to be debt claims, such as claims for dividends that had been declared but not paid before bankruptcy, should now be classified as equity claims. Justice Fitzpatrick also found that a judgment obtained on such a claim before bankruptcy continued to be an equity claim.

[523] While it is not entirely clear, it appears that the Trustee interpreted *Re Bul River* and other cases that reached similar conclusions as authority for the proposition that any claim arising out of an agreement that calls for the sharing of profits with a bankrupt should be regarded as an equity claim.

[524] However, none of the cases relied upon by the Trustee dealt with the issue raised in this case, which is whether non-bankrupt joint venturers were equity creditors of a bankrupt joint venturer who held legal title to property that was beneficially owned by all the joint venturers.

[525] The scheme of the *BIA* requires the Trustee to make a determination of the property of the bankrupt that is divisible among its creditors. In making that determination the Trustee must comply with the provisions of s. 67(1)(a), which excludes property held in trust for another person from being distributable.

[526] Section 140.1 is found in the Scheme of Distribution Portion of Part V of the *BIA*. The Scheme of Distribution set out in the *BIA* applies only to claims against the property of a bankrupt that is divisible among its creditors. It does not convert property that is not divisible into property that is, or otherwise affect entitlement to that property.

[527] The inability of the Trustee to divide property held in trust for another person among the creditors of a bankrupt under the *BIA* was recognized in *Royal Bank of Canada v. North American Life Assurance Co.*, [1996] 1 S.C.R. 325 at 357:

> 62 However, the trustee is barred from dividing two categories of property among creditors: property held by the bankrupt in trust for another person (s. 67(1)(a)), and property rendered exempt from execution or seizure under provincial legislation (s. 67(1)(b)). While such property becomes part of the bankrupt's estate in the possession of the trustee, the trustee may not exercise his or her estate distribution powers over it by reason of s. 67.

[528] Section 140.1 therefore has no application to such property.

[529] This however does not mean that the common law rule that precludes the payment of the capital of a business until all creditors of the business have been paid does not apply to joint ventures. The question is how it should properly be applied.

Applicable common law rule

[530] The long-standing common law rule was that all of the creditors of an insolvent business must be paid before any capital could be recovered. In these reasons I have referred to the rule as a common law rule even though it is an equitable rule, which originated in the Chancery Division.

[531] Before 2009, persons holding capital in a bankrupt business had no right to file any claim in a bankruptcy. Section 140.1 allowed equity holders to make a claim but maintained the rule that such a claim was postponed to the claims of creditors.

[532] Despite this change I am of the view that the common law rule against distribution of capital until all creditors claims are paid remains in force.

[533] I reach this conclusion for two reasons. First, the 2009 amendments do not contain a complete definition of an equity creditor, stating only that an equity creditor is a person who makes a claim in respect of an equity interest. The definition of equity interest referred to above applies only to corporations. There is a similar definition of an equity interest in an income trust. There is however no statutory

definition in the *BIA* of an equity claim that arises out of other business arrangements.

[534] In addition, a statute should be presumed to have modified the pre-existing common law only if it does so in clear language: *Glenko Enterprises Ltd. v. Keller*, 2007 MBCA 7 at para. 47; *Jackson v. Canadian National Railway*, 2013 ABCA 440 at para. 37. I therefore conclude that Parliament intended that the existing rule would remain in force in situations to which s. 140.1 is not applicable.

[535] The common law rule is described in *Sukloff v. A.H. Rushforth & Co. Estate*, [1964] S.C.R. 459. A person who contributes to the capital of a business carried on for their joint benefit has no right to receive any return of its capital until all of the creditors of the business have been paid in full. For this principle, Justice Ritchie quoted *Halsbury's Laws of England*, 3rd ed., vol. 2 (London: Butterworths, 1964) at 495:

> If a person advances money to another not by way of loan but as a contribution to the capital of a business carried on for their joint benefit, the person who has made the advance, even though he is not a partner in the business and has received no share of the profits as such, is debarred from proving in the bankruptcy of the recipient of the money in competition with the creditors of the business.

[536] The principle set out in *Halsbury's* and applied by Justice Ritchie is derived from the English Court of Appeal decisions of *In Re Meade*, [1951] Ch. 774, and *In Re Beale* (1876), 4 Ch. D. 246. *In Re Meade* involved a couple that entered into a horse-riding academy business together. The wife provided her husband with funds to buy the academy and necessary equipment with the understanding that the couple would live on the grounds they had purchased, operate the academy, and live off its proceeds. It was ruled that this contribution could not be considered a loan, but rather a contribution to the capital of a business enterprise in which she had an interest. As such, the wife was "no more entitled, as against the ordinary creditors of the business, to prove in respect of her contribution than the proprietor is entitled to prove in respect of his" [emphasis added].

[537] This principle was also applied in *Laronge Realty Ltd v. Golconda Investments Ltd.* (1986), 7 B.C.L.R. (2d) 90 (B.C. C.A.), and accurately summarized in the headnote as follows:

> If the advances were not loans the case would not be within s. 110 (now s. 139) but would be governed by the common law rule that if a person advances money to another as a contribution to the capital of a business carried on for their joint benefit, the person who has made the advance, even though he is not a partner in the business and has received no share of the profits as such, is debarred from proving in the bankruptcy of the recipient of the money in competition with the creditors of the business.

[538] The only businesses that can be said to have been carried on by the plaintiffs and the Bankrupts for their joint benefit are the joint ventures – not the Bankrupts themselves. I am satisfied that, as joint venturers, the plaintiffs' capital contributions at issue in this litigation were to the joint ventures (and their businesses, the Project) and *not* to the Bankrupts. Thus, they are not equity creditors pursuant to the common law rule described above.

[539] I reviewed the terms of the JVAs in detail earlier in these reasons. The parties to all of the written joint venture agreements in issue agreed that each joint venturer owned a proportionate share of the assets acquired for the joint venture as its separate property. That agreement meant that the interest of the Bankrupts pursuant to those agreements was limited to the Bankrupts' proportionate share as set out in each joint venture agreement. In the case of 690174 that interest is limited by the terms of the 2007 JVA.

[540] The Bankrupts acquired no further divisible interest by virtue of other joint venturers' contributions or by holding the property of the joint venture in trust. While they managed the business of completing the Project, they were not themselves the business.

[541] The position of the joint venturers in the case at bar can usefully be compared to that of partners, in spite of significant differences between partnerships and joint ventures. If a partner in a partnership becomes bankrupt, only that partner's interest in the partnership is subject to division among its creditors. The property of the partnership ceases to be held jointly and becomes held as tenants in common. In

L.W. Houlden & C.H. Morawetz, *Bankruptcy and Insolvency Law of Canada*, 4th ed. (Toronto: Thomson Reuters Canada) G§162(10) [Houlden & Morawetz], the editors state the proposition as follows:

> If only one member of a partnership becomes bankrupt, the trustee becomes tenant in common with the solvent partner in of the assets of the firm: *Ex parte Stoveld* (1823), 1 Gl. & J. 303.

[542] In a partnership, the property of the partnership is owned by the partnership. Unlike a partnership, a joint venture cannot own property. The property employed in the joint venture is owned in the manner specified in the joint venture agreement. As stated in *Canlan,* the property is usually owned jointly by the joint venturers in accordance with their proportional interests, as in the case at bar. Similar to a partnership, it is only the interest of the bankrupt joint venturer that vests in its trustee. To the extent that the bankrupt holds legal title to assets of the joint venture in trust for nor bankrupt joint venturers, s. 67(1)(a) precludes that property from being divided among the creditors of the bankrupt joint venturer.

[543] *Re Abacus Cities Ltd.* (1984), 50 C.B.R. (n.s.) 289 (Alta. Q.B.), was the only authority referred to by counsel for the Trustee in support of his submission that solvent joint venturers are equity creditors of a bankrupt joint venturer. The Trustee's case book included a quotation from Houlden & Morawetz suggesting that the advances made in that case were contributions of equity. However, the case does not support that proposition.

[544] *Re Abacus Cities* arose out of the bankruptcy of a real estate developer that syndicated properties through the use of joint venture agreements. The applicants, who had purchased units from Abacus Cities, sought a declaration that payments they had made to Abacus were received subject to a trust in their favour. The Court held that the amounts received were not subject to a trust and that no debtor-creditor relationship existed with regard to most of their claims. However, the reason for that finding was that the Court found the amounts claimed had been advanced to Abacus for services to be rendered, which it had in fact provided. Therefore, nothing was owing in respect of those payments. This is made clear at para. 13:

> 13 In *Thorne Riddell Inc. v. Rolfe* (1982), 44 C.B.R. (N.S.) 219, 22 Alta L.R. (2d) 76, 19 B.L.R. 98, 44 A.R. 161 (Q.B.), the court dealt with a similar enterprise of Abacus based on a set of similar agreements. The issue in that case was whether the developer/clients were personally responsible to trade creditors for obligations made by Abacus. It was held that Abacus was best classified as an independent contractor. In reasons for judgment I stated it was not subject to control as to the details of the work to be performed. It was not engaged in a master and servant relationship. I see little difference between the position of Abacus and that of a house builder who is employed "merely to accomplish certain results and is not otherwise subject to his employer's control in the manner of performance". I follow that decision in this case. The relationship between Abacus and the developer/client is governed by the extensive agreements into which they entered.

[545] It is to be noted that in *Re Abacus Cities,* the Court did find that a small amount from the advances had not been earned by Abacus Cities and allowed the applicants to prove as unsecured creditors for that amount. There is no suggestion that the Court considered those claims to be equity claims. The decision therefore does not support the Trustee's submission.

The Garchas' claim

[546] The Garchas' rights are set out in the 2007 JVA, which expressly recognizes their beneficial ownership of a proportionate share of the assets of the 2007 JVA.

[547] I repeat that the Trustee wrongly assumes that the Garchas are seeking to share in the property of 690174 that is divisible among its creditors. That is not the case. As I stated earlier in these reasons, the Garchas are seeking to recover their own property by tracing it into the proceeds of sale of the subdivided lots. The property they are seeking does not and never did belong to 690174.

[548] The fact that the Garchas' interest was beneficial rather than legal does not change their ownership of it: *Foskett*, quoted at para. 277. I find that the property they seek to recover falls squarely within s. 67(1)(a) and is therefore not divisible among 690174's creditors. Section 140.1 therefore does not apply to it.

[549] It is also relevant to note that a trustee has no better claim to property than the bankrupt had before bankruptcy except in certain circumstances such as deemed trusts created by provincial statutes, or legislation requiring registration of security interests such as conditional sales agreements.

[550] This principle was reiterated in *Lefebvre v. Tremblay (Trustee of)*, 2004 SCC 63. Although *Lefebvre* dealt with an issue arising out of the *Civil Code of Quebec*, S.Q. 1991, c. 64, Justice Lebel described the underlying principle as applicable to both the *Civil Code* and common law:

> 37 When the trustee takes control or becomes seised civil law of the universality of property defined in s. 67 *B.I.A*., his or her seisin is limited to the property in the debtor's patrimony. Apart from the special powers accorded by law to the trustee, as representative of the creditors, to restore the patrimony to be liquidated in its entirety, the trustee has no more rights with respect to the debtor's property than did the debtor, of whom the trustee remains the successor in this regard. This principle is well established in relation to the application of s. 67 *B.I.A*. It was laid down by Judson J. in *Flintoft v. Royal Bank*, [1964] S.C.R. 631 (S.C.C.), at p. 634. More recently, Iacobucci J. confirmed the validity of the principle in *Giffen*. In my view, the trustee has no greater interest in the property under his or her responsibility than that of the bankrupt, unless otherwise provided for by legislation (*Giffen*, at para. 50).

[551] The passage from *Flintoft v. Royal Bank of Canada*, [1964] S.C.R. 631 at 634, referred to in *Lefebvre* states as follows:

> 7 We are not concerned here with the rights of a purchaser for value without notice of the proceeds of the sale of the bank's security. It is true that s. 63 of the *Bankruptcy Act* avoids in favour of the trustee the assignment of book debts held by the bank because of defective registration. Subject to this, the trustee has no higher rights than the bankrupt and he takes the property of the bankrupt merely as a successor in interest and not as an innocent purchaser for value without notice. He takes the property of the bankrupt subject to the express trust created by the agreement noted above, which, in my opinion, cannot be characterized as an assignment of book debts in another form. When these debts, the proceeds of the sale of the s. 88 security, come into existence they are subject to the agreement between bank and customer. As between these two the customer has nothing to assign to the bank. The actual assignment of book debts which was signed does no more than facilitate collection. Any other assignment, whether general or specific, of these debts by the customer to a third party would fail unless the third party was an innocent purchaser for value without notice.
>
> [Emphasis added]

[552] The Garchas' were not participating in 690174's profits from the 2007 Joint Venture. The profits to which they were entitled arose out of their own proportionate beneficial ownership interests in the 2007 Joint Venture and not from the property of 690174.

[553] I therefore find that the Garchas' claims are not equity claims but, as explained in *Foskett,* are simply claims to recover their own property.

Rajpreet and Mr. Mattu's claims

[554] The claims advanced by Rajpreet and Mr. Mattu are distinguishable from the Garchas' claims because they are based on oral joint venture agreements that do not contain the express statement of beneficial ownership found in the 2007 JVA.

[555] The Trustee submits that the claims of Mr. Mattu and Rajpreet fall under s. 140.1 of the *BIA* because the relationship they allege is one in which they were to share profits with the Bankrupts.

[556] In my view this submission is based on the misunderstanding of the nature of an equity investment that similarly afflicts the Trustee's argument regarding the Garcha claim. If Mr. Mattu and Rajpreet had contributed capital to the Bankrupts their claims to that capital would have been postponed to other claims against the Bankrupts. However, the business to which they contributed capital was the Project, which was being pursued by the November 2010 and 2011 Joint Ventures. It is the creditors of *that business*, not of the Bankrupts, that must be paid in full before any of the joint venturers, including the Bankrupts, are entitled to any return of capital.

[557] The Trustee appears to have conflated the concepts addressed by ss. 139 and 140.1 of the *BIA* by emphasizing the concept of sharing profits and overlooking the critical question of whether Mr. Mattu and Rajpreet can be said to have contributed to the capital of the Bankrupts' business. Section 139 postpones the claims of creditors who advance money to a borrower under a contract which provides for the lender to share in the profits of a business being carried on by the bankrupt. However, the Trustee does not rely on s.139, nor could he, because the advances made by Rajpreet and Mr. Mattu were not loans.

[558] Thus, I find that Rajpreet and Mr. Mattu have not advanced equity claims to the property of the Bankrupts. Rather, their claims relate to the property of the Project over which I have granted a remedial constructive trust.

[559] Another troubling implication of the Trustee's analysis is it would mean that anyone who enters into a joint venture with a company that subsequently becomes bankrupt would have its right to the capital and profits of the joint venture postponed to the claims of all of the creditors of the bankrupt joint venturer. The Trustee has cited no authority for such a result. The critical error that the Trustee has made is the same as the one described by Justice Blair in *Lester & Orpen Dennys Limited v. Canadian Broadcasting Corporation*, [1991] O.J. No. 1399 (Ont. C.J.). In that case, the Trustee made precisely the same argument being made by the Trustee in this case; that is that the CBC, which had entered into a joint venture with the bankrupt should have its claim against the bankrupt postponed because the joint venture called for a sharing of profits. Justice Blair succinctly disposed of the argument as follows:

> 6 . . . . What is being claimed here is a share of the profits of a joint-venture agreement that arises through a written contract between Lester & Orpen Dennys Limited and CBC, not the share of profits of Lester & Orpen Dennys Limited itself. This fact distinguishes the circumstances from those which existed in the Meade case and the *Sukloff* case . . .
>
> [Emphasis added]

[560] The terms of the joint venture under consideration in *Re Orpen Dennys* were not specified in the decision. It appears that the appellant in that case was entitled to a share of the royalties from a publication rather than a proportionate share of the assets. Nevertheless, Justice Blair had no difficulty in finding that the appellant was not seeking any share of the bankrupt's profits.

[561] I therefore find that the claims of Mr. Mattu and Rajpreet are not equity claims and that 140.1 has no application to those claims.

Property of the Bankrupts subject to a constructive trust is not divisible among its creditors

[562] On the facts I have found, Mr. Mattu and Rajpreet are each entitled to a constructive trust over the proceeds of the Project on the basis of the Bankrupts' breach of fiduciary duty with respect to the funds they advanced to Jaswant and on the principles of unjust enrichment.

[563] Property which has been found to be subject to a constructive trust may be property held in trust for the purposes of s. 67(1)(a) of the *BIA*, depending upon when the constructive trusts came into existence.

[564] In *Ellingsen (Trustee of) v. Hallmark Ford Sales Ltd.,* 2000 BCCA 458, Justice Donald, writing for the majority, held that in a bankruptcy the court has the discretion to impose a constructive trust effective prior to the bankruptcy:

> [38] I turn to consider the issue of timing: can the constructive trust be imposed prior to the bankruptcy? In order for the remedy to have any practical effect, it must be imposed before the bankruptcy, otherwise s. 67(1)(a) of the *BIA* could not operate. Support for the proposed timing can be found in *Rawluk v. Rawluk*, 1 [1990] S.C.R. 70 at 91:
>
> > It is important in this respect to keep in mind that a property interest arising under a constructive trust can be recognized as having come into existence not when the trust is judicially declared but from the time when the unjust enrichment first arose. As Professors Oosterhoff and Gillese state, "the date at which a constructive trust arises…is now generally accepted to be the date upon which a duty to make restitution occurs" (Oosterhoff and Gillese, *A.H. Oosterhoff: Text, Commentary and Cases on Trusts* (3rd ed. 1987), at p. 579). Professor Scott has stated in *Law of Trusts*, op. cit., at pp. 323-4, that:
> >
> > > The beneficial interest in the property is from the beginning in the person who has been wronged. The constructive trust arises from the situation in which he is entitled to the remedy of restitution, and it arises as soon as that situation is created. … It would seem that there is no foundation whatever for the notion that a constructive trust does not arise until it is decreed by a court. It arises when the duty to make restitution arises, not when that duty is subsequently enforced.

[565] In *BNSF Railway Company v. Teck Metals Ltd.*, 2016 BCCA 350 at para. 76, Justice Newbury also held that the court has discretion to determine whether the trust arises at the time of judgment or some earlier date, such as when the act that gave rise to the trust occurred.

[566] I note that in the passage from *Rawluk* referred to in both cases, Justice Cory, writing for the majority, stated that he agreed completely with the statements of the authors of the texts quoted by him that the trust arises at the time when the duty to make restitution arises and not when declared by the court.

[567] In this case, I also find that the constructive trusts arose prior to the Bankruptcies. The trust in favour of Rajpreet arose at the latest when the 2011 Joint Venture was formed without expressly providing him with an interest in it. With respect to the first $200,000 that 0892995 provided to Panorama, it arose when Panorama and Jaswant used those funds as part of the deposit for the purchase of Lot 5.

[568] Similarly, the remedial constructive trust in favour of Mr. Mattu arose when Jaswant used the funds he received from Mr. Mattu without ensuring that Mr. Mattu's proprietary interest in the Project was protected, or at the latest when the November 2010 JVA was executed without protecting Mr. Mattu's rights under his oral joint venture agreement with Jaswant.

[569] However, the Trustee submits that in a bankruptcy context, a remedial constructive trust is only available over property that would otherwise form part of the bankrupt's estate in cases where it is necessary to do so to remedy debtor misconduct. In this regard he relies on *Credifinance Securities*.

[570] This argument has no merit with respect to the Garchas' claim for the reasons I have already given. The remedy the Garchas have been granted is the right to trace their own property into the lots created by the Project. As set out in *Foskett*, the remedy they have been granted is not based on an exercise of the court's discretion to order a remedial constructive trust but on a recognition of their property rights.

[571] The remedy granted to Mr. Mattu and Rajpreet was discretionary, with the imposition of a remedial constructive trust based both upon the need to remedy wrongful conduct and unjust enrichment.

[572] However, in my view, *Credifinance Securities* does not assist the Trustee. In that case, the issue before the court was whether a claimant who had been defrauded by the bankrupt could assert a constructive trust over funds that had been frozen in civil proceedings commenced prior to the bankruptcy. A judge of the Ontario Superior Court of Justice ordered that the claimant was entitled to assert a trust claim over the funds.

[573] On appeal, Justice Laforme set out what the court considered to be the relevant test:

> 33 There is no question that the remedy of constructive trust is expressly recognized in bankruptcy proceedings. Both the case law and authors of texts make this clear, although the test for proving the existence of a constructive trust in a bankruptcy setting is high: L.W. Houlden & Geoffrey Morawetz, *Houlden and Morawetz Bankruptcy and Insolvency Analysis* (Toronto: WL Can, 2011) at F§5(1). The authors add this at F§5(8): "A constructive trust will ordinarily be imposed on property in the hands of a wrongdoer to prevent him or her from being unjustly enriched by profiting from his or her wrongful conduct" (citations omitted).
>
> 34 *Ascent*, a case decided by an Ontario Registrar in Bankruptcy, is a case that demonstrates the type of circumstances that can make a case extraordinary. I found this case to be very instructive.
>
> The Registrar in *Ascent* held that in its role as the arbiter of commercial morality, the Bankruptcy Court can rely on equitable principles, "even at the expense of the formulaic aspects of the *BIA* scheme of distribution": para. 17.
>
> 36 An example of commercial immorality is described in *Ascent* as being where a bankrupt and its creditors benefit from misconduct by the bankrupt which was the basis upon which the property was obtained. The Registrar held that to permit an estate to retain the property in such circumstances amounts to an unjust enrichment, and the court can impose a constructive trust on an estate's assets to remedy the injustice. Furthermore, "it matters not which assets are consumed to remedy this": para. 18.
>
> 37 Thus, a constructive trust in bankruptcy proceedings can be ordered to remedy an injustice; for example, where permitting the creditors access to the bankrupt's property would result in them being unjustly enriched. The prerequisite is that the bankrupt obtained the property through misconduct. The added necessary feature is that it would be unjust to permit the bankrupt and creditors to benefit from the misconduct.

[574] I have some difficulty in reconciling the above comments with the clear statements of the Supreme Court of Canada in *Lefebvre* and *Flintoft* that a Trustee in Bankruptcy has no better claim to property than the bankrupt, unless the *BIA* expressly provides otherwise.

[575] However, in any event, the remedy I have granted to Mr. Mattu and Rajpreet is based on Jaswant’s misconduct. Refusing to impose a constructive trust would result in the creditors benefitting from Jaswant’s wrongful acts. The facts before me therefore fall clearly within the circumstances described above. The funds Mr. Mattu and Rajpreet provided made a material contribution to the successful completion of

the Project. Jaswant agreed that the funds they provided to him entitled them to an interest in the Project.

[576] In this case, I find that depriving Mr. Mattu and Rajpreet of their beneficial rights in the Project would result in an unjust enrichment of the general body of creditors, whose recovery in the bankruptcy comes almost entirely from the success of the Project: *Redstone* at para. 71.

[577] I therefore see no reason why s. 67(1)(a) of the *BIA* should not apply to the remedial constructive trusts imposed by this judgment. The property over which a constructive trust has been ordered is property held in trust and is therefore not divisible among the creditors of the Bankrupts.

[578] Some of the confusion that has arisen in these proceedings may have originated from the nature of the proofs of claim filed by the plaintiffs. I agree with the Trustee that those claims ought to have been filed pursuant to s. 81(1) of the *BIA.* However, the Trustee has acknowledged that he understood the basic nature of the claims and his counsel has indicated that the Trustee is content to have this issue decided in these proceedings.

[579] I am also satisfied that even if the plaintiffs had filed such claims pursuant to s. 81(1), the Trustee would have disputed them pursuant to that section of the *BIA.*

[580] In summary I find that the claims of the Garchas, Mr. Mattu, and Rajpreet are not postponed to the claims of the general body of creditors of the Bankrupts and that it is only the proportionate beneficial interests of the Bankrupts in the 2007 and 2011 Joint Ventures that form part of the assets divisible among the general body of creditors.

[581] However, in accordance with *In Re Meade,* all direct creditors of the Project must be paid in full before any proceeds are distributed to the joint venturers, Rajpreet, and Mr. Mattu.

[582] If I am wrong in concluding that Rajpreet and Mr. Mattu are entitled to a constructive trust or have entered into a joint venture agreement with the Bankrupts,

this does not mean that they are equity creditors. Following *Re Orpen Dennys*, in such a case they would be entitled to rank as unsecured creditors because they did not contribute any capital to the Bankrupts. The Trustee therefore erred in law in disallowing their claims on that ground in any event.

Remedies

Garcha remedies

[583] The Garchas seek an order that they receive a proportionate share of the gross proceeds of sale of the subdivided lots. As I understand their submission there are two aspects to their claim.

[584] Firstly, they seek a proportionate share of the gross proceeds from the Project that are attributable to Lot 1. Their position is that the only permissible deduction from those gross proceeds should be their pro rata share of $1,750,000, the principal amount of the second PMIC mortgage. They calculate that share to be 7/22 of that amount, or $556,818. They submit that they should not be responsible for any share of Project development costs because they were not given the opportunity to approve those costs and because the Trustee has refused to provide an accounting of them.

[585] Secondly, on the theory that a rogue trustee should be deprived of any benefit obtained from a breach of fiduciary duty, they also seek a share of the gross proceeds from the Project arising out of the lots attributable to Lots 2 to 5 which would otherwise be payable to the other 2011 Joint Venturers, whom they allege are liable for knowing assistance or knowing receipt.

[586] In my view these claims are overreaching and exceed the remedy to which the Garchas are entitled and which would compensate them adequately.

[587] I find that the Garchas are entitled to their proportionate share of the net proceeds of the Project that are attributable to Lot 1, as determined by the 2007 JVA. Pursuant to those terms the Garchas are entitled to 7/22 of the proceeds from 22 lots subdivided from Lot 1.

[588] The Project resulted in the creation of 81 saleable lots. 690174's 28.5% interest in the 2011 Joint Venture equates to 23 of those lots. The 2007 JVA entitles 690174 to the proceeds of sale of the extra lot. The Garchas' entitlement is therefore 7/23 of 28.5% of the net proceeds of the Project.

[589] 690174 is entitled to 1/23 of that 28.5% interest, which will of course form a part of its estate. There is also evidence that 690174 acquired the interest of one of the other joint venturers. If that is the case 690174 is entitled to the proceeds attributed to that interest.

[590] An assessment of the amount to which the Garchas are entitled can only be made after adjustments to the net revenue for unpaid project expenses and a determination of responsibility for specific amounts previously paid by the Trustee, which include the amount paid to satisfy the Virk Mortgage.

[591] Counsel for the Garchas argued that this case called for a remedy that has a prophylactic purpose, as discussed in *Wang v. Wang*, 2020 BCCA 15 at paras. 56-59. Counsel argues that 690174 and the persons who knowingly assisted its breaches of fiduciary duty should be deprived of any benefit from those breaches to deter fiduciary faithlessness and preserve the integrity of the fiduciary relationship. He submits that Jaswant acted dishonestly and that dishonesty warrants the more draconian remedy of full disgorgement of any benefits he or those who are also responsible for his actions have obtained.

[592] I have concluded that awarding this remedy would be unfair to the other parties who have contributed to the success of the Project and would in effect unjustly enrich the Garchas. On this aspect of the case I do think that the interests of the creditors of the Bankrupts should be taken into account.

[593] A fiduciary that breaches its duty must account for what it acquired in consequence of its breach. However, in *3464920 Canada Inc. v. Strother*, 2007 SCC 24, Justice Binnie cautioned against making harsh awards out of all proportion to the actual behaviour of the wrongdoer:

> 88 The Court of Appeal, despite its observation that the accounting remedy itself should not become "an instrument of injustice" (*BCCA #1*, at para. 52), nevertheless concluded that the "accounting period" should be open-ended:
>
> > After much anxious consideration, I have therefore concluded that Mr. Strother must be required to account for and disgorge to Monarch all benefits, profits, interests and advantages he has received or which he may hereafter be entitled to receive, directly or indirectly (i.e., through a corporation, trust, or other vehicle), from or through any of the Sentinel Hill Entities.
> >
> > (*BCCA #1*, at para. 61, per Newbury J.A.)
>
> An accounting of profits is an equitable remedy and, as La Forest J. noted in a different context:
>
> > ... equity is not so rigid as to be susceptible to being used as a vehicle for punishing defendants with harsh damage awards out of all proportion to their actual behaviour.
> >
> > (*Hodgkinson v. Simms*, at p. 444)
>
> 89 To the same effect, the High Court of Australia noted in *Warman International Ltd. v. Dwyer* (1995), 128 A.L.R. 201 (Australia H.C.), at pp. 211-12:
>
> > ... the stringent rule requiring a fiduciary to account for profits can be carried to extremes and ... in cases outside the realm of specific assets, the liability of the fiduciary should not be transformed into a vehicle for the unjust enrichment of the plaintiff.
>
> In *Warman* itself, the Court found that two years was the appropriate period for which defendants should be ordered to account. From the profits so determined, an allowance for the expenses, skill, expertise, effort and resources contributed by the defendants was to be deducted.

[594] In addition, the general rule is that the reasonable and necessary expenses incurred to earn the benefit are deductible from the amount that must be accounted for: *Strother* at para. 97. The method of assessment sought by the Garchas is contrary to this rule.

[595] In addition to the above claims, the Garchas seek to recover their proportionate share of what they allege was the secret profit of $300,000 obtained by 690174 in relation to the assignment fee paid to 688350. As I am satisfied that there was in fact no secret profit obtained from this payment, no relief is granted in respect of this claim.

[596] The Trustee submits that the Garchas' entitlement should be adjusted to account for their under-contribution to the carrying costs of the Lot 1 Acquisition

Mortgage. The Trustee has calculated that shortfall as $174,962.49, based on the Garchas being responsible for 7/23 the carrying costs.

[597] I have some difficulties with this submission. The Garchas' entitlement is approximately 8% of the net proceeds of the Project, for which they have already contributed approximately $475,261. Given the unsatisfactory state of the accounts kept for the Project, I am not satisfied that the Garchas have not paid their share of the costs of the Lot 1 Acquisition Mortgage.

[598] The Garchas' contribution can usefully be compared to the confirmed contribution of Ranjit and Svender of less than $400,000, which resulted in them being entitled to 7.17% of the net proceeds. The Trustee has also allocated the same percentage to Wills and Dale, who contributed only $25,000 to Project costs.

[599] I therefore find that the 7/23 of 690174's share of the net proceeds of the Project are beneficially owned by the Garchas, and that they are entitled to be paid that amount from the funds held in trust.

[600] I have not addressed the entitlement of the non-party 2007 Joint Venturers in these reasons. During the trial, counsel for the Trustee indicated that some form of accommodation has been reached with some or all of those 2007 Joint Venturers. I however am not in a position to determine whether they are entitled to the same remedy as the Garchas, principally because I do not know the extent to which they gave their informed consent to 690174's actions.

[601] However, to the extent that other 2007 Joint Venturers are entitled to benefit from this judgment, I consider it just and equitable that the Garchas be entitled to indemnification for a proportionate share of their legal expenses, on a solicitor-client basis, from such recoveries. I give the Garchas leave to pursue this claim at the hearing to be held to consider costs issues generally. If the Garchas intend to pursue such an order, they must give notice to the non-party 2007 Joint Venturers.

Mattu and Rajpreet remedies

[602] While I am satisfied that Rajpreet and Mr. Mattu are entitled to the remedy of a constructive trust, the more difficult question is how to determine its amount.

[603] Mr. Mattu submits that I should find all of the members of the November 2010 JVA to be bound by Jaswant's agreement with him; that is, that he should receive a share of the proceeds based on his relative contributions to the Project. He argues that his agreement with Jaswant predates the November 2010 JVA and, in any event, that Jaswant had the actual authority to amend its terms to further the development of the Project by making an accommodation for him in it.

[604] However, there are formidable practical difficulties in determining the actual amounts contributed to the Project by the various parties. This is mainly attributable to the chaotic state of the Project accounting. It is however also attributable to the informality of the dealings between Rajpreet, Mr. Mattu, and Jaswant.

[605] Unfortunately, I found the Trustee's spreadsheets of limited utility in determining the amounts actually contributed by the parties. One of my major difficulties arises out of the methodology used by the Trustee in analyzing the flow of funds. The Trustee used the accounting principle of first in first out, known as FIFO. The legal equivalent of FIFO is the Rule in Clayton's Case. That case created a legal presumption that funds withdrawn from an account are deemed to be drawn from the first funds paid into the account.

[606] However, in cases involving a breach of fiduciary duty, the operative legal rule is the Rule in Hallett's Case arising from the decision in *Re Hallett's Estate*, (1880) 13 Ch. D. 696 (Eng. C.A.), which held that when a trustee mixes its own funds with those of its beneficiaries, it is deemed to use its own funds for non-trust related expenses and the trust funds for the purpose for which it received them.

[607] This principle was applied by Justice Grauer in *Re 0409725 B.C. Ltd.*, 2015 BCSC 1221:

> 20 But trusts do not evaporate because the trust property disappears. It is here, then, that the breaches of trust come to the fore. As noted in my second Reasons, there can be no doubt that all of the monies paid by the

> owners of the various projects at issue were funds that, prior to the bankruptcy, were impressed with trusts by section 10(1) of the *BLA*. Those trusts remained until the beneficiaries were paid. The problem is that any attempt after the bankruptcy to assess what remains in trust on a project-by-project basis is frustrated by Odenza's breaches (paying sub trade claims of one job with funds received from other jobs). On a FIFO approach, the effect would be to limit the trusts to the last few standing — last in, still there.
>
> 21 But the law is quite clear that FIFO is the wrong approach to the distribution of mingled trust funds where the trust claims exceed the amount available. The correct approach is to distribute the funds pro rata: *Law Society of Upper Canada v. Toronto Dominion Bank (1998)*, 42 O.R. (3d) 257 (Ont. C.A.) and *Ontario (Securities Commission) v. Greymac Credit Corp*. (1986), 55 O.R. (2d) 673 (Ont. C.A.), upheld [1988] 2 S.C.R. 172 (S.C.C.).
>
> 22 The law also provides that where a trustee acts in breach of trust in the mingling and spending of trust and non-trust funds, he is deemed to have spent his own money first, and trust money last: *Hallett's Estate, Re (1880)*, 13 Ch. D. 696 (Eng. C.A.).

[608] This principle is important in this case because equity presumes that Jaswant used Rajpreet's and Mr. Mattu's funds in the Project and his own funds for purposes not related to it.

[609] An additional consideration is that dividing the revenue strictly on the basis of financial contributions would make no provision for the considerable contribution that Jaswant's abilities and efforts as a developer have made to the success of the Project.

[610] I have therefore concluded that the appropriate remedy in this case is one that permits Rajpreet and Mr. Mattu to obtain a fair share of the proceeds of the Project but does not completely replace the existing legal interests set out in the 2011 JVA.

[611] A defining feature of equitable remedies is their responsiveness to the facts of a particular case. As stated in *Kerr v. Baranow*, 2011 SCC 10 at para. 71, "[t]he Court has often emphasized the flexibility of equitable remedies and the need to fashion remedies that respond to various situations in principled and realistic ways". Given that equitable remedies are so dependent on the facts, significant judicial discretion is permitted (indeed, required) in fashioning them. Such discretion encompasses "the full gamut of available remedies": *Cadbury Schweppes Inc. v. FBI*

Foods Ltd., [1999] 1 S.C.R. 142 (S.C.C.) at 179-180. Imposition of a constructive trust is recognized as one of such remedies: *Soulos* at 236.

[612] Any method of determining an appropriate remedy for Rajpreet and Mr. Mattu will be to a certain extent arbitrary. Given the deplorable state of the Project accounts (which have made it virtually impossible to determine the amount most parties contributed to the total Project costs), the inconsistency between the various agreements that Jaswant made, the recognition that Jaswant's efforts did bring the Project to a successful completion, and the failure of Mr. Mattu and Rajpreet to document their agreements with Jaswant, I have concluded that the fairest way to compensate them is to impose a constructive trust in their favour over a portion of the net proceeds of the Project.

[613] I originally considered awarding Rajpreet and Mr. Mattu an amount equal to their investment plus a reasonable rate of return on it. However, I have concluded that such a division would not reflect the risks that they would have known they were taking by investing in the Project. Taking all of the above factors into account, I have concluded that the most appropriate way to compensate Rajpreet and Mr. Mattu is to adjust the proportionate shares of the parties to the 2011 Joint Venture to reflect their investment.

[614] The best comparable to use to determine a fair share for Rajpreet and Mr. Mattu is the amount that Grewal Management paid to acquire its 14.25% interest in the Project. My view is that the appropriate amount to use is the initial amount that Grewal Management paid to acquire its interest in Lot 5, which was approximately $1,690,000. Rajpreet's investment was $800,000, which is 47% of that investment. I have determined Mr. Mattu's investment to be $1,062,000, which is approximately 62.3% of Grewal Management's investment. Applying these percentages to the 14.25% of the profits obtained by Grewal Management results in granting Mr. Mattu 9% and Rajpreet 6.8% of the net revenue from the Project.

[615] I find that it is appropriate to charge that amount pro rata among the members of the 2011 Joint Venture, including the 28.5% interest of 690174. The evidence in this case demonstrates that the members of the 2011 Joint Venture did not

contribute sufficient funds to finance the acquisition and development costs of the Project. That deficiency was made up in large part by the funds contributed by Mr. Mattu and Rajpreet. All of the 2011 Joint Venturers have therefore benefitted from Mr. Mattu and Rajpreet's contributions.

Project Accounting Issues

[616] The final determination of the amounts to which the parties are entitled requires decisions on a number of the accounting issues. Some of these issues were raised by the Trustee in his Ninth Report to the Court and his Submission Re Adjustments and Reallocations. Some arise from the findings I have made.

[617] In Exhibit 175, the Trustee estimated total project recoveries of $15,441,090.52. After deduction of amounts disbursed by the Trustee, the balance held in trust as of February 28, 2018, was $10,118,804.25. These deductions included approximately $2,775,000 in Trustee's fees and legal expenses (the "Trustee Costs"). The amount of the Trustee Costs has increased significantly since February 2018. In Schedule 2 of Summary 1, the Trustee estimated $3,500,000 in Trustee Costs to the completion of the file.

[618] The parties are agreed that the there will be a further hearing to address the issues of costs and how the Trustee Costs should be allocated. For convenience I will refer to this hearing as the "Accounting Hearing"

[619] I also wish to emphasize that I regard the Vendor Trust Accounts as having been set up for convenience only and that they are of no assistance in determining the final entitlements of the Parties. I will however decide certain allocation issues in these reasons.

The Virk Mortgage

[620] In Exhibit 175, the Trustee allocated the full amount paid to satisfy the Virk Mortgage to 690174's Vendor Trust Account. It is obvious from my decision that 690174 holds all but a 1/23 interest in the Project in trust for the 2007 Joint Venturers and that it is therefore inappropriate to use 690174's share of the proceeds to pay the Virk Mortgage. Jaswant acknowledged at all times that the Virk

Mortgage was his responsibility. I have also found that Jaswant and Parmjit were engaged in a joint enterprise with respect to the Project. It follows from this finding that Parmjit must also bear responsibility for the Virk Mortgage. Panorama should also bear a proportionate share of the amount of this payment based on Jaswant's complete control of its affairs. The proportionate shares chargeable should be based on the relative share of the proceeds payable to these parties under the 2011 JVA. However, no portion should be charged to Ranjit and Svender's or Grewal Management's share of the proceeds.

[621] In addition, my finding that Wills and Dale hold their interest as nominees for Jaswant implies that they are responsible for their proportionate share of this cost. However, it would not be fair to charge Wills and Dale's share of the proceeds with a portion of the Virk Mortgage payout because that issue was not raised during the trial. I give the parties leave to make submissions on that issue at the Accounting Hearing.

Payout of Acquisition Mortgages

[622] During the course of the trial I expressed concern about the discrepancy between the amounts contributed to the Project by the 2011 Joint Venturers and their proportionate entitlements set out in the 2011 JVA. I need not repeat those concerns. The Trustee's explanation for the discrepancy was that the proportionate interests set out in the 2011 JVA were based on the size of the Lots contributed to the Project by the 2011 Joint Venturers. He reasoned that because the Lots were acquired by the persons contributing them at different times and in different market conditions, it made sense to determine the proportionate interest from the size of the contributed Lots rather than the amount paid for them.

[623] However, this analysis overlooks a crucial consideration. Each of the Lots contributed was encumbered by an Acquisition Mortgage which was paid out from the proceeds of the first WSCU Mortgage, which itself was ultimately paid proportionately by the 2011 Joint Venturers from lot sales.

[624] This resulted, for example, in Panorama receiving 14.25% of the Project in exchange for contributing a share of a Lot that it had purchased from the proceeds of an Acquisition Mortgage which was paid off by all of the 2011 Joint Venturers based on their proportionate shares in the 2011 Joint Venture. In contrast, Grewal Management paid cash for its share of Lot 5 and received only a partial refund of that price, almost as an afterthought, when the order to pay the WSCU Mortgage was signed. Yet, Grewal Management obtained an identical 14.25% interest in the Project.

[625] I have concluded that this result is inconsistent with the terms of the 2011 JVA, which clearly contemplated that expenses should be borne in accordance with the proportionate interests of the 2011 Joint Venturers. To address this issue, I find that the amounts paid in March 2012 to pay out the Acquisition Mortgages, as well as the cash payment to Grewal Management and the amount paid to discharge the Ludu Mortgage, should be regarded as an advance payment of Project profits to the 2011 Joint Venturers who benefitted from them. This will require an adjustment to the final amount distributable to take those benefits into account. For clarity, the amount paid to retire the Ludu Mortgage should be regarded as an advance distribution to Jaswant and Parmjit. I have also concluded that the amounts paid to pay the Virk Mortgage should be regarded as an advance distribution of profits to Jaswant, Parmjit, and Panorama.

[626] It seems to me that these adjustments may notionally increase the profits from the Project by an amount equal to the March 2012 payouts, but I will leave it to the Trustee to make this adjustment.

[627] In addition, the accounts will have to be adjusted to take into account the remedies I have granted to Rajpreet and Mr. Mattu. This means that the amount available for distribution to the signatories to the 2011 JVA will be 84.2% of the net Project proceeds. It would seem that this will result in a pro rata reduction of the share of the proceeds payable to each of the 2011 Joint Venturers. However, the parties may make submissions at the Accounting Hearing on this issue.

Other adjustments with respect to specific payments

[628] I agree with the manner in which the Trustee has allocated the payments or credits (all as set out in Schedule 2 to Summary 2 of Exhibit 175) to the B & B Contracting liability of $410,734.62; the PTT Lien of $37,110.34; the direct Project creditors of $113,981.43; the May 16, 2012, deposit to 690174's WSCU account on May 16, 2013; and the Buckley Hogan payment to the City of Surrey and Project completion costs.

[629] I do note that the direct Project creditors amount was increased to $115,583.15 in the Trustee's Submission Re Adjustments and Reallocations, delivered after the close of the evidence. The correct figure should be used for this adjustment.

[630] I do not agree that any adjustment is appropriate for carrying costs from November 15, 2010, to the date of payout of the Acquisition Mortgages. Even though the beneficial ownership of the Lots may have changed on November 15, 2010 I find that the parties who contributed the Lots remained responsible for their carrying costs on the capital that they provided to the Project. They should not be regarded as Project costs.

[631] It may be that some joint venturers made payments on Acquisition Mortgages that were not their responsibility. If that is the case an adjustment as between the venturer who paid and the venturer who was responsible may have been appropriate. However, that is an adjustment that falls outside of the Project accounting and the scope of these proceedings.

Indirect Project creditors

[632] The Trustee also suggests that what he referred to as indirect Project creditors should share directly in the distribution of Project profits. These appear to refer to amounts borrowed by the Bankrupts that were in turn used by the Bankrupts to make three categories of payments relating to the Project as set out in Summary 5 of Exhibit 175:

1. Project mortgage payments

2. Project land purchases

3. Project costs

[633] Project mortgage payments appear to be payments made on the Acquisition Mortgages, which I have already found are not Project costs. I have made the same finding with respect to Lot acquisition costs, referred to above as Project land purchases.

[634] The third category is difficult to identify because Summary 5 does not provide the dates on which the payments were made or specifics regarding what they were made for. For example, page 2 of Summary 5 shows that the Trustee allowed a claim of $322,227.50 from Manjit Bains as an unsecured creditor of Jaswant. Of this amount, $48,954.26 was allocated to Project costs. $46,000 of that amount was paid to Buckley Hogan, Jaswant's lawyers. No other details are provided.

[635] Despite this concern, I am prepared to credit the Bankrupt estates with payments made for Project costs, apart from land acquisition and carrying costs, after November 15, 2010, from funds borrowed from their creditors to the extent that such payments can be proven on a balance of probabilities. Any such payments should be credited to the Bankrupt that made them and not the entity from whom they were borrowed. The persons who provided that credit did not provide it to the Project but to the Bankrupts. If the parties cannot agree on the amounts of such payments they may make further submissions at the Accounting Hearing.

[636] I am also of the view that the amounts shown as an advance from Raveen to 690174 must be closely scrutinized because I do not recall Raveen ever having testified to making any such advance. However, if 690174 can demonstrate that it made a payment to B & B Contracting of $199,098.49 for Project costs from funds it borrowed, it is entitled to the appropriate credit for that payment, taking into account its obligation to bear a proportionate share of that expense.

Accounting Process

[637] It is difficult to conceptualize the most useful method of determining the combined issues of Project accounting and allocation of Trustee Costs.

[638] After much consideration I have concluded that the accounting should follow the following process:

1. The Trustee should prepare an initial accounting of the Project incorporating the directions and decisions I have made without deducting anything for legal costs or Trustee Costs. This accounting should show the amounts that each of the parties is entitled to from the Project based on my reasons and the terms of the 2011 JVA.

2. The Trustee will also update Exhibit 175 to include all Trustee Costs to the present, including charges that have not yet been presented for approval

3. The parties will then make submissions on how the Trustee Costs should be satisfied, including on the issue of the extent to which the interests of the non-bankrupt parties should be used to pay the Trustee Costs.

Summary of Orders

[639] In summary, I make the following orders:

1. Each 2007 Joint Venturer is the beneficial owner of its proportionate share of the assets of the 2007 Joint Venture.

2. Jaswant and 690174 breached their fiduciary duties to the 2007 Joint Venturers by:

    i. Permitting financial charges that arose from 690174’s outside dealings to be registered against Lot 1.

    ii. Registering other financial charges against Lot 1 to provide security for obligations incurred by 690174 in pursuit of its separate business interests.

iii. Purporting to transfer the beneficial ownership of Lot 1 to the members of the November 2010 and 2011 Joint Ventures.

iv. Entering into the Land Swap Agreement, which transferred a significant portion of Lot 1 to the Anglican Diocese of New Westminster in exchange for land that was utilized for the benefit of the 2011 Joint Venturers without obtaining the informed consent of the 2007 Joint Venturers.

v. Executing a mortgage over Lot 1 to secure the WSCU financing that was used to finance the Project for the exclusive benefit of the 2011 Joint Venturers.

3. Panorama, Parmjit, Ranjit, and Svender are liable to the 2007 Joint Venturers in knowing assistance and knowing receipt.

4. The Garchas' claim for punitive damages is dismissed.

5. Jaswant breached an *ad hoc* fiduciary duty to Rajpreet and Mr. Mattu regarding the funds they advanced towards the Project.

6. The Vendor Trust Accounts are to be consolidated into one trust account to be disbursed in accordance with these reasons and the directions made on the accounting.

7. 22/23 of the 28.5% share of the net proceeds of the Project allocated to 690174 in the 2011 JVA is held in trust for the members of the 2007 JVA and 7/22 of that share is held in trust for the Garchas.

8. Grewal Management's claim is dismissed.

9. 9% of the net proceeds of the Project are subject to a constructive trust in favour of Mr. Mattu and 6.8% are subject to a constructive trust in favour of Rajpreet. The parties may make submissions at the Accounting Hearing as to how these trusts should affect their entitlement to the remaining 84.2% of Project proceeds.

10. The amount paid to satisfy the Virk Mortgage is to be borne proportionately by the Bankrupts and Parmjit.

11. The appeals of the disallowances of the claims are allowed, and the claims of the appellants are disposed of by the orders I have made in the trials of their claims.

12. There will be a declaration that the claims of the plaintiffs are not equity claims.

13. There will be an Accounting Hearing to address the issues identified in these reasons as requiring further submissions and to determine the costs of these proceedings.

Sewell J.

TAB 2

CITATION: *10390160 Canada Ltd et al. v. Casey et al*., 2022 ONSC 628
COURT FILE NO.: CV-21-00671326-00CL and CV-21- 00664534-0000
DATE: 2022-01-28

SUPERIOR COURT OF JUSTICE – ONTARIO (COMMERCIAL LIST)

RE: 10390160 CANADA LTD., 1139950 B.C. LTD., 2545142 ONTARIO INC., 2659154 ONTARIO INC., 2576725 ONTARIO INC., 2593273 ONTARIO INC., 5001047 ONTARIO INC., AVONDA REALTY AND DEVELOPMENT INC., BEISTONE INC., CAN SUCCEED INTERNATIONAL INVESTMENT CORP., LIZ INVESTMENT INC., LIQIN WANG, ZHZH HOLDING LTD., BV TOWER INVESTMENT LIMITED PARTNERSHIP and BV TOWER INVESTMENT LIMITED PARTNERSHIP II, Plaintiffs

AND:

DANIEL CASEY, HOMELIFE NEW WORLD REALTY INC., SIMON YEUNG, SAM YEUNG, CRESFORD (YORKVILLE) GP INC., CRESFORD HOLDINGS LTD., CRESFORD DEVELOPMENTS, 2611029 ONTARIO INC., 154290 ONTARIO LTD.; CRESFORD (ROSEDALE) DEVELOPMENTS INC., 9615334 CANADA INC., YSL RESIDENCE INC., CRESFORD CAPITAL CORPORATION, YG LIMITED PARTNERSHIP, VOX (YONGE WELLESLEY LTD.), 50 CHARLES STREET LIMITED, 50 CHARLES STREET LIMITED PARTNERSHIP, 42 CHARLES STREET LIMITED, 42 CHARLES STREET LIMITED PARTNERSHIP, 1000 BAY STREET LIMITED, 1000 BAY STREET LIMITED PARTNERSHIP, ROSEDALE DEVELOPMENTS INC., 59 HAYDEN STREET LIMITED, 62-64 CHARLES STREET LIMITED, CRESFORD EQUITIES LIMITED, CRESFORD FINANCIAL LIMITED, CRESPO, EAST DOWNTOWN REDEVELOPMENT PARTNERSHIP, 48 YONGE STREET INC. CRESBUILD.CRESFORD REAL ESTATE CORPORTATION; OAKLEAF CONSULTING LTD., OAK BRANCH TRUST, LONG BRANCH TRUST, 2103546 ONTARIO LIMITED, RED BIRCH PROPERTIES INC., WHITE BIRCH PROPERTIES INC., 2402193 ONTARIO LIMITED, 1594290 ONTARIO LIMITED, and CRESFORD EQUITY INC., Defendants

AND BETWEEN:

ERIC YIN WING CHAN, LINDA YEE HAN CHAN, 2638006 ONTARIO INC., 2504670 ONTARIO INC., PINE POINT INTERNATIONAL INC., 2595683 ONTARIO INC., and NEW WORLD INVESTMENTS 1988 LIMITED, Plaintiffs

AND:

DANIEL CASEY, 154290 ONTARIO LTD., CRESFORD (ROSEDALE) DEVELOPMENTS INC., CRESFORD (YORKVILLE) GP INC., CRESFORD DEVELOPMENTS, 9615334 CANADA INC., YSL RESIDENCE INC., CRESFORD CAPITAL CORPORATION, YG LIMITED PARTNERSHIP, 48 YONGE STREET INC., VOX (YONGE WELLESLEY LTD.), 50 CHARLES STREET LIMITED, 50 CHARLES STREET LIMITED PARTNERSHIP, 42 CHARLES STREET LIMITED, 42 CHARLES STREET LIMITED PARTNERSHIP, 1000 BAY STREET LIMITED, 1000 BAY STREET LIMITED PARTNERSHIP, 62-64 CHARLES STREET LIMITED, ROSEDALE DEVELOPMENTS INC., 59 HAYDEN STREET LIMITED, CRESFORD EQUITIES LIMITED, CRESFORD FINANCIAL LIMITED, CRESPO, CRESBUILD, CRESFORD REAL ESTATE CORPORATION, CRESFORD EQUITY INC., 2103546 ONTARIO LIMITED, OAKLEAF CONSULTING LTD., RED BIRCH PROPERTIES INC., WHITE BIRCH PROPERTIES INC., 1594290 ONTARIO LIMITED, EAST DOWNTOWN REDEVELOPMENT PARTNERSHIP, LONG BRANCH TRUST, OAK BRANCH TRUST, 2492193 ONTARIO LIMITED and 2611029 ONTARIO INC., Defendants

BEFORE: Penny J.

COUNSEL: *John J. Adair and Robert Stellick* for the Plaintiffs in Action No.: CV-21-00671326-00CL

Shara N. Roy, Aaron I. Grossman and Sahar Talebi for the Plaintiffs in Action No.: CV-21-00664534

Jeffrey Larry and *Daniel Rosenbluth* for the Defendants in both Actions

HEARD: December 10, 2021

ENDORSEMENT

[1] The Plaintiffs in these two actions are investors in units of a limited partnership whose purpose was the development of a luxury condominium project at 33 Yorkville Avenue in Toronto.

[2] In this motion, the plaintiffs seek a *Mareva* injunction against Daniel Casey, Oakleaf Consulting Ltd., Cresford Rosedale Developments Inc. (“Rosedale Developments”), East Downtown Redevelopment Partnership (“EDRP”), Long Branch Trust and Oak Branch Trust (these are collectively the “Mareva defendants”). This motion was first made on notice to the defendants on May 3, 2021, three months after the action was commenced.

[3] To obtain a *Mareva* injunction, the moving party must establish:

(1) a strong *prima facie* case, meaning, in this context, that the plaintiffs are clearly right, or even that they are almost certain to win;

(2) the defendant has assets in the jurisdiction;[1]

(3) there is a serious risk that the defendant will remove or dissipate its assets before judgment can be obtained;

(4) the plaintiff will suffer irreparable harm if the injunction is not granted (in the context of a *Mareva* injunction this is usually the same as item 3 above, in the sense that the inability to enforce any judgment obtained at trial due to the removal or dissipation of assets *is* the irreparable harm); and,

(5) the balance of convenience favours granting the injunction, in the sense that the harm suffered if the injunction is not granted will exceed the harm that will be suffered if it is.

The moving party must also give a meaningful undertaking as to damages. See e.g. *Chitel v. Rothbart* (1982), 39 O.R. (2d) 513 (C.A.); *Borelli v. Chan*, 2017 ONSC 1815, 137 O.R. (3d) 382 (Div. Ct.), at paras. 17-20, 60.

[4] The main issues in dispute on this motion are the existence of a strong *prima facie* case and risk of dissipation. For the reasons that follow, I am not satisfied that either threshold has been met in the circumstances. The motion is dismissed.

Background

[5] What has been referred to as the "Cresford group" or just "Cresford" consists of the corporate defendants other than Homelife (which is unrelated).

[6] As of 2018, Cresford had five active condominium projects under way in Toronto:

i. Clover Project: a two-tower development owned by the Clover on Yonge Inc.;

ii. Halo Project: a 39-storey tower owned by 480 Yonge Street Inc.;

iii. Yorkville Project: a two-tower development owned by 33 Yorkville Residences Inc.;

iv. YSL Project (sometimes "YG"): owned by 9615334 Canada Inc. and YSL Residences Inc.; and

v. CASA III: a condominium project owned by 50 Charles Street Limited.

[1] In *Borelli v. Cha*n, 2017 ONSC 1815, a majority of the Divisional Court held that in certain circumstances, this requirement could be waived. This is not an issue here.

[7] Each project was owned by a separate special purpose legal entity which held legal title to the land and took steps to develop and build the project. The special-purpose entity was the general partner of a limited partnership which beneficially owned the project.

[8] The directing mind of Cresford is Mr. Casey. He is the president and sole director of each of the Cresford companies, with control over the decisions and affairs of each company. He is also the sole trustee of the two Trusts, the beneficiaries of which are Casey's wife and children.

[9] Corporate beneficial ownership and control of the Cresford group resides with Oakleaf and the two Trusts. Oakleaf owns (through a holding company) 100% of the shares of the key holding and operating companies within the Cresford group. The Trusts own 100% of Oakleaf.

[10] The key operational companies (in addition to each project company) were EDRP and Rosedale Developments. EDRP was the manager of the Cresford companies. Its function was to manage the projects, pay employees, receive management fees, and perform related functions. Rosedale was the financial arm and financial clearing house for the Cresford group.

[11] The plaintiffs' claims are for breach of contract, breach of fiduciary duty, knowing assistance in a breach of trust, negligent misrepresentation and unjust enrichment.

[12] For the purposes of this motion, the plaintiffs focus on the following core allegations:

• All Cresford companies were completely dominated and controlled by Casey.

• Casey caused the Cresford companies to engage in a "shell game" in which money was wrongfully moved from one project to another on an as-needed basis, contrary to the provisions of the limited partnership agreements and alleged representations made, and in breach of the defendants' duties to the plaintiffs/unitholders. All of the projects are now under some form of receivership or court supervision, including the Yorkville project. As a result, the unitholders' investment in the Yorkville project appears to be entirely without value.

• Casey operated the Cresford group in complete and total disregard for the corporations' separate legal personality and his and his companies' fiduciary duties. This course of conduct was for the benefit of the three entities that own Cresford's interest in the projects - Oakleaf and the two Trusts.

• Finally, Casey and the entities he controls have engaged in asset dissipation in order to defeat his creditors.

[13] The *Mareva* defendants take the position that, with the possible exception of the claim against Casey on his personal guarantees, no strong *prima facie* case has been established against any of the remaining defendants. They further take the position that there is no

evidence of removal or dissipation of assets with intent to defeat judgment creditors (or at all).

The Main Issues

[14] The two main issues in dispute at the hearing of the motion were:

(1) whether a strong *prima facie* case has been made out against any *Mareva* defendant (other than Casey) and;

(2) whether intentional acts of dissipation have been established sufficient to warrant granting the extraordinary remedy of a *Mareva* injunction.

Analysis

Strong Prima Facie *Case*

[15] The first issue arises from the requirement, in order to grant the extraordinary remedy of a *Mareva* injunction, that the moving party satisfy the court that it has a strong *prima facie* case. Strong *prima facie* case means, in this context, that the plaintiff must show that it is "clearly right" in its allegations made against the responding party in the action or that it is "almost certain to succeed at trial" in respect of those allegations: *SLMsoft.Com Inc. v. Rampart Securities Inc. (Bankruptcy)*, 2004 CanLII 6329 (Ont. S.C.) at para. 14, leave to appeal refused (2005), 78 O.R. (3d) 521 (Div. Ct.).

[16] The plaintiffs advance basically two arguments in support of their claim that their investments in the Yorkville project were wrongfully diverted to other purposes: a) a number of intercompany transfers appearing in Cresford ledgers and bank statements; and, b) the findings of this Court in receivership proceedings involving the Yorkville and YSL projects.

Intercompany Transfers

[17] At the heart of the plaintiffs' allegations is the assertion that Cresford improperly caused money invested by the plaintiffs in the Yorkville project to be diverted to other projects in an ultimately unsuccessful effort to keep those other projects afloat when Cresford ran into financial difficulties.

[18] The plaintiffs acknowledge that, prior to receiving disclosure of Cresford's financial records in the course of this motion, their only evidence with respect to intercompany transfers came from Cresford's former president, Maria Athanasoulis (who, the plaintiffs concede, was not particularly involved in the companies' financial affairs).

[19] More damaging to the reliability and credibility of Ms. Athanasoulis' evidence than her admitted lack of familiarity with Cresford's financial affairs, however, are the further revelations that, in 2019 while employed as Cresford's president, Athanasoulis was working with a third party investor group on a potential acquisition of Cresford's YSL

project. Athanasoulis resigned from Cresford in January 2020 at a time when those negotiations were ongoing. Immediately after Athanasoulis' resignation, two of Cresford's key secured lenders received a letter purportedly authored and signed by Cresford's CFO, David Mann. Each letter contained allegations of wrongdoing against Cresford, including allegations of "financial fraud" and a "fraudulent plan". Athanasoulis commenced an action against Cresford shortly thereafter, alleging extensive improprieties against the Cresford defendants. Cresford investigated the origins of the two letters purportedly from Mr. Mann who denied having written or sent them. Cresford determined that Athanasoulis was the real author of these letters. In the face of the evidence uncovered by this investigation, Athanasoulis admitted in her cross-examination on this motion that she had surreptitiously authored and sent these two letters, forging Mann's signature in the process.

[20] In any event, one transaction was originally identified in Athanasoulis' evidence - a journal entry where $2 million was transferred from the Yorkville project to Rosedale and then on to the YSL project. According to Athanasoulis, "there would be no legitimate business reason for that transfer of $2 million from 33 Yorkville to YSL." In Cresford's responding affidavit, Mann testified there was nothing improper about this transfer and that it represented repayment of an intercompany loan Rosedale Developments had advanced to the Yorkville project at an earlier stage of the development when full financing was not yet in place.

[21] This transaction was then subject to additional examination by independent accounting experts. Other than an arithmetic error in calculating the total amount owed, the expert evidence confirmed that funds substantially in excess of $2 million were owed by the Yorkville project to Rosedale Developments at the time the $2 million transfer was made.

[22] In their factum, however, and with the benefit of production of additional financial records following the cross examinations, the plaintiffs now argue that there are "dozens" of "impugned" intercompany transfers. These are set out in a chart at para. 31 of the plaintiffs' factum, listing 11 intercompany transfers identified from the Yorkville project's ledger. Unfortunately, the record is devoid of further evidence on these transfers beyond the plaintiffs' lay attempt at matching up certain entries taken from the Yorkville project's ledgers and Rosedale Developments' bank statements between April 2018 and January 2020. What these entries show is that the Yorkville project made 11 transfers to Rosedale Developments and that Rosedale Developments, soon after, then made transfers to other Cresford projects in sometimes similar amounts.

[23] Cresford relies on Mann's evidence generally, to the effect that these were all repayments of loans advanced by Rosedale Developments at an earlier stage of the development, and that there is no contrary evidence. There is no challenge to this evidence, as far as it goes.

[24] The plaintiffs respond to this, however, by arguing that there is also no evidence documenting any of these "loans" or how Cresford knew or was able to confirm specifically how much was owed to whom when the transfers were made from the Yorkville project's account to Rosedale Developments. This is why the plaintiffs refer to these transfers as Cresford's "shell game" which wrongfully diverted funds away from the

Yorkville project in violation of contractual and other alleged duties the plaintiffs plead were owed to them by the *Mareva* defendants. Indeed, the plaintiffs go so far as to say, in their factum, that the existence of a legitimate debt to be repaid is "largely irrelevant," and "what is important about Cresford's 'loan theory' is that Cresford did no contemporaneous analysis" to determine the existence of the payable at the time of the transfer.

[25] There are several problems with this argument. First, the allegation of the absence of contemporary analysis pre-transfer is effectively speculation. This allegation was not put to Mann or any other witness. We simply do not know what, if any, transaction by transaction analysis was done or, if not, why not.

[26] Second, it is not clear why this would matter. If, as the available evidence seems to suggest, there was more intercompany debt owed to Rosedale Developments than the amount of any transfer out of the Yorkville project at any given time, what difference would the lack of specific contemporary analysis actually make? And, to the extent there is a suggestion that the transfers exceeded the amount of any legitimate intercompany loans, that has not, in any event, been proved to the high threshold required on a *Mareva* injunction.

[27] The elevated threshold for the merits test in a *Mareva* injunction matters here. The absence of loan documentation and any apparent lack of due diligence and monitoring and recording about the state of intercompany obligations, together with the suggestion that these transfers, and the financial state of Cresford's projects generally, were kept, for example, from its secured lenders, raises strong suspicions, even perhaps a triable issue about the propriety of these transfers. However, the evidence and the manner in which it has come before the court does not permit the conclusion that the plaintiffs' claims, with the possible exception of the claims on Casey's personal guarantees, are "almost certain to succeed".

[28] Finally, it must be acknowledged that the entities with which the plaintiffs had direct contact and contractual ties are the 33 Yorkville LP and its general partner. These entities are not *Mareva* defendants. The *Mareva* defendants (leaving aside Casey and his personal guarantees) are all "upstream" entities with which the plaintiffs had no contact and, at the time of their investments, effectively no knowledge.

[29] The plaintiffs' theory of liability against these upstream entities in particular, in negligent misstatement, breach of fiduciary duty, knowing assistance and unjust enrichment, all appear to stem from Casey's overall control of the Cresford group of companies, including the two Trusts. The issues of negligent misstatement and unjust enrichment were not really the subject of evidence on this motion at all. The focus seems to be on the allegations of knowing assistance in a breach of trust.

[30] The leading authority on knowing assistance claims against related parties is van Rensburg J.A.'s dissenting reasons in *DBDC Spadina Ltd. v. Walton*, 2018 ONCA 60, 419 D.L.R. (4th) 409, rev'd 2019 SCC 30, [2019] 2 S.C.R. 530, which were endorsed by a unanimous Supreme Court of Canada on appeal from the majority judgment of the Court of Appeal.

[31] Justice van Rensburg would have dismissed the related party claims in that case because the "participation" element had not been established. Noting that the authorities require "specific harmful conduct" by the stranger to the trust, van Rensburg J.A. explained that the plaintiffs did not point to any independent conduct by the related companies establishing their "participation" in the principal's breach of fiduciary duty except to repeat the same allegations made against the principal. These related corporations under the control of the principal may have "participated" in the general sense in the fraudulent scheme when money was moved to and from their accounts, and been "conduits" or "been used by [Walton] in the overall fraud", but "that does not equate to their participation in the dishonest breach of fiduciary duty": see *DBDC Spadina*, at paras. 217-21.

[32] *DBDC Spadina* stands for the proposition that "something more" is required for a knowing assistance claim beyond the mere receipt of funds or being used as a conduit in the overall breach of trust. The mere fact that Cresford entities may have been subject to the same directing mind, it seems to me therefore, is, standing alone, insufficient to establish an independent basis for the claim of knowing assistance in a breach of trust. In this case, as noted above, there is insufficient evidence to establish, to the standard required for a *Mareva* injunction, a basis for concluding the plaintiffs are almost certain to succeed in their claims against the *Mareva* defendants (other than Casey on his personal guarantees) on this basis as well.

Findings of the Court in Other Proceedings

[33] The plaintiffs rely on certain findings in *BCIMC Construction Fund Corporation et al. v. The Clover on Yonge Inc.*, 2020 ONSC 1953, 78 C.B.R. (6th) 299, the March 30, 2020 decision of Justice Koehnen appointing a receiver over Cresford's Clover, Halo and Yorkville projects. The test on an application for the appointment of a receiver is whether it is "just and convenient" to do so.

[34] After becoming aware of the Athanasoulis claim against Cresford, the secured creditors of these projects retained PwC to conduct an investigation. PwC reported that it had found evidence that significant cost overruns had been concealed from the creditors, contrary to the financial performance and management covenants contained in the loan documents. This consisted of: a) instead of injecting its own funds, Cresford borrowed money from a third party and used that loan as "equity" in the project; b) the projects maintained two sets of books - the first set, used to support advances under the loans, showing costs that were consistent with the construction budgets which had been presented to the lenders, and a second set recording increases over the approved construction budgets which were not shown to the lenders; and, c) to help hide the increased costs, Cresford sold units to suppliers at substantial discounts to their listing prices.

[35] Despite having more than three weeks to respond to the allegations of improper financial practices reported by PwC, the debtors failed to do so, remaining "completely silent about the allegations" at the return of the application. In these circumstances, Koehnen J. concluded "I can only assume that the allegations are true and were, at all material times, known to and accepted by senior management".

[36] The plaintiffs also rely on the findings of Justice Dunphy in *YG Limited Partnership and YSL Residences (Re)*, 2021 ONSC 4178, 93 C.B.R. (6th) 109. In that case, YSL sought approval of a proposal in bankruptcy which was opposed by limited partnership unit holders in the YSL project. The issue in that case was whether the proposal was reasonable and calculated to benefit the general body of creditors under s. 59(2) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "BIA"), and whether the proposal met the common law requirement of having been made in good faith. Justice Dunphy rejected YSL's proposal in bankruptcy, finding:

• The YSL general partner was in breach of its fiduciary duties to the limited partnership by advancing a bankruptcy proposal that would involve a breach of the YSL limited partnership agreement and see substantial payments to Cresford in advance of any payments to the unit holders, i.e., payment of $38 million to non-arm's length parties related to the YSL general partner.

• The YSL general partner tried to keep relevant information from the YSL LP investors and was looking for a solution, not to meet its obligations to the partnership but, rather, "to secure the optimal outcome" for the Cresford group of companies generally, such that "good faith took a back seat to self-interest".

• Intercompany advances between the YSL project and various other Cresford companies recorded on the general ledger of the YSL limited partnership were "sporadic," "non-interest bearing without any defined term or maturity date," and were not evidenced by any loan documents. In the circumstances, for the purposes of any proposal under the BIA, those transfers had to be considered contributions of equity by the Cresford companies, not debt.

[37] In both cases, the legal framework and the test for granting relief were different. The allegations, facts and circumstances were also different. Koehnen J.'s decision appointing a receiver involved allegations of concealing significant cost overruns from the secured creditors. In this case, the plaintiffs do not say that the allegations vis-à-vis the secured lenders in the receivership case also involved breaches of obligations owed to the unit holders. Rather, the unit holders' allegation is that their investment dollars were diverted to other entities and projects in contravention of obligations owed to them. There was no evidence about this before Koehnen J. Further and in any event, it is clear from Koehnen J.'s reasons that the findings he made were without the benefit of any evidence from Cresford responding to PwC's investigation report.

[38] Dunphy J.'s decision involved a different project altogether and different investors in limited partnership units. The breaches of duty found against the general partner of YSL arose out of the nature of the proposals made by YSL in its NOI proceedings which, Dunphy J. found, would, if approved, have involved a breach of the limited partnership agreement. Dunphy's J.'s findings about intercompany transfers were not that the transfers themselves were improper (that issue was not put before him) but that these alleged obligations between YSL and Cresford related parties ought not to take precedence over *bona fide*, arm's-length equity holders in terms of recoveries under the proposal. Dunphy

J. essentially sent YSL back to the drawing board to come up with a better, more equitable proposal. That, I understand, was done and a revised proposal was made addressing Dunphy J.'s concerns. This proposal was approved by the court on July 16, 2021.

[39] Read and considered in proper context, the findings of the court in these other proceedings do not constitute strong *prima facie* evidence that Cresford improperly diverted investor funds from the Yorkville project to other projects and Cresford entities for improper purposes. As with the earlier evidence, these decisions raise suspicions and may contribute to there being a triable issue but do not rise to the level necessary to support the stringent merits test for a *Mareva* injunction.

Conclusion on Strong *Prima Facie* Case

[40] In summary, the central issue in this case will be whether Cresford's financial collapse and the resulting loss of the unit holders' equity in the Yorkville project, was caused by breaches of contractual or other duties allegedly owed by Cresford to the unit holders. At the heart of the alleged wrongful conduct is the so-called "shell game" engaged in by Cresford through the intercompany transfers. Were these transfers improper or justified? Answering that question will involve careful and detailed forensic analysis of the transfers, the sources and destinations of the funds and whose money was being transferred, when, where and why.

[41] Unfortunately, that analysis has not been done, even on a preliminary basis for the purposes of this motion. This is because, as explained above, the scope of these allegedly improper transfers only came out in the plaintiffs' factum. There is essentially no evidence (that is, first hand fact or expert forensic evidence) about these transfers apart from a listing of a selection of entries from various ledgers and bank statements which have been produced in the context of this motion. For the same reason, there has been no cross-examination about the circumstances and purpose of these now-impugned transactions. While it may be said that these intercompany transactions raise suspicions warranting further investigation, and even a triable issue, the high threshold required for the grant of a *Mareva* injunction has not been reached.

Intention to Remove or Dissipate Assets to Defeat Judgment

[42] Even if I were wrong about the merits test and was prepared to accept that a strong *prima facie* case of improper diversion of investor funds out of the Yorkville project had been made out, there is a more fundamental impediment to the grant of a *Mareva* injunction in this case.

[43] The *sine qua non* of the *Mareva* injunction is the requirement that there be evidence of an intention to put assets beyond the reach of the court for the purpose of defeating any judgment that might ultimately be granted in the plaintiff's claim. This requirement has been variously described in decisions of Canadian courts commencing with *Chitel v. Rothbart* (1982), 39 O.R. (2d) 513 (C.A.) and *Aetna Financial Services Ltd. v. Feigelman*, [1985] 1 S.C.R. 2. As stated by Estey, J. in *Aetna Financial,* at pp. 24 and 27:

> The overriding consideration qualifying the plaintiff to receive such an order as an exception to the *Lister* rule *is that the defendant threatens to so arrange his assets as to defeat his adversary,* should that adversary ultimately prevail and obtain judgment, in any attempt to recover from the defendant on that judgment.
>
> …
>
> In summary, the Ontario Court of Appeal recognized *Lister* as the general rule, and *Mareva* as a "limited exception" to it, the exceptional injunction being available only where there is a real risk that the defendant will remove his assets from the jurisdiction or dissipate those assets *to avoid the possibility of a judgment*… [Emphasis added.]

[44] The Court of Appeal has explained that "the purpose of the defendant is the decisive question. In other words, it is only if the purpose of the defendant when removing assets from the jurisdiction or the dissipating or disposing of them is for the purpose of avoiding judgment that a *Mareva* injunction should be issued": *R. v. Fastfrate* (1995), 24 O.R. (3d) 564 (C.A.), applied in *RBC Dexia Investor Services Trust v. Goran Capital Inc.*, 2016 ONSC 1138, at para. 11(b).

[45] While the risk of dissipation can, like other facts, be inferred from the circumstances of the impugned conduct, the overriding consideration is always whether the defendants are dealing with their assets in such a way as to put them out of the reach of the plaintiffs if the claim is successful: *Sibley & Associates LP v. Ross*, 2011 ONSC 2951, 106 O.R. (3d) 494, at paras. 62-64; *HZC Capital Inc. v. Lee*, 2019 ONSC 4622, at para. 83.

[46] The plaintiffs rely on the following circumstances in support of the necessary proof of dissipation that must be shown (or inferred):

(a) Cresford's attempts to "strip" assets out of the projects through court supervised receivership /insolvency proceedings;

(b) Cresford's failure to disclose that it will receive about $5 million from the sale of YSL assets under the revised and now approved proposal in the YSL NOI proceedings;

(c) the overall context of the alleged "shell game" in which Cresford moved money about without regard to the legal separation of its various corporate entities;

(d) the purchase of a house in Toronto for Casey's son; and

(e) the transfer of two boats and two parcels of Ontario land owned by Casey personally to a corporation owned or controlled by him.

[47] I am unable to agree that these allegations amount to the necessary proof of an intention to place assets beyond the reach of the court.

[48] The fact that Cresford tried to bargain for certain benefits in the context of receivership/insolvency proceedings, and was unsuccessful is doing so, cannot be regarded as evidence, circumstantial or otherwise, of an intention to place assets beyond the reach of the court. This argument stands the "dissipation" requirement on its head; the court had and asserted jurisdiction over the very assets in question. There was nothing secret about what Cresford was doing. The court was not prepared to countenance any "sweet" deals for Cresford and rejected Cresford's attempts to obtain such benefits.

[49] The plaintiffs acknowledge that the $5 million allocation to Cresford under the YSL proposal is not being paid to Cresford at all but is earmarked for payment to certain YSL creditors – specifically to third-party sureties for that project. The sureties are a group of arm's-length third party creditors which have crystallized claims in relation to bonds and insurance policies they issued to secure the deposits made by purchasers of condominium units. Those claims have been identified and described in the various Receiver's reports filed with the court. The total amount of these claims is estimated to be in excess of $35 million.

[50] The sureties' claims include a claim under an indemnity agreement with Rosedale Developments, Cresford Holdings Limited, Casey, and 33 Yorkville Residences Inc. Other than 33 Yorkville Residences Inc., which is in receivership, each of those indemnitors is a defendant to this action.

[51] The evidence is that the sureties are bona fide arm's-length creditors with clear entitlements under their indemnity agreements. The sureties tendered an affidavit on this motion from Terry Michalakos. Mr. Michalakos confirmed that Cresford agreed from the outset to assign its entire interest in YSL proceeds to the sureties in order to settle the sureties' claims under the indemnity agreement. The sureties will, of course, be prejudiced if the assignment of these proceeds is restrained as a result of this motion.

[52] I am unable to regard payment in reduction of a crystalized debt and indemnity as a dissipation of Cresford assets or as giving rise to an inference that Cresford is trying to place assets beyond the reach of the court.

[53] I have already reviewed the evidence concerning the alleged "shell game". The problem with the plaintiffs' argument in the context of the dissipation requirement is that, even if it were true, there is absolutely no evidence that any of these transfers involved taking funds out of the jurisdiction or otherwise dissipating assets with the intention of defeating future judgment creditors. The evidence is, so far as it goes, that these payments were made in an effort to keep various other Cresford projects afloat.

[54] The Yorkville project is in receivership. PwC is the court-appointed receiver. PwC has filed reports with the court. There is no evidence that PwC has ever come across evidence that Cresford was stealing investors' money from the Yorkville project. Indeed, counsel for the plaintiffs specifically wrote to counsel for PwC to ask about this very issue. The response, obviously qualified by the scope of PwC's mandate, was that no transactions

were identified that warranted further investigation. The relevant passage of the response states:

> Investigation of Payments: The Receiver conducted an initial review of the 33 Yorkville cost ledgers. No transactions were identified by the Receiver in the course of that review that, in the Receiver's view in the context of the receivership and in light of the Receiver's mandate and directions received from creditors, warranted further investigations. No specific investigation was made of Rosedale Developments Inc., which is not subject to the receivership.

[55] The necessarily qualified nature of this response is by no means a complete defence to the plaintiffs' allegations. However, the fact that an officer of the court, appointed to report to the court on the financial affairs of the Yorkville project, has found no transactions warranting further investigation, is not supportive of the plaintiffs' claims either to a strong *prima facie* case or that assets have been improperly placed beyond the reach of the court.

[56] And finally, the evidence that Casey caused a home to be purchased in Toronto for his son, or that Casey transferred relatively modest assets to a company controlled by him is, on its face, not evidence of dissipation. These are and remain assets in the jurisdiction. They are known. If, at the end of the day, it is proved there were transfers for no or inadequate consideration, they are in any event liable to be set aside. As noted earlier, the core purpose of the *Mareva* injunction is to protect against defendants who intend to remove assets from the jurisdiction or otherwise render assets unavailable for execution. Here, the transfers complained of largely relate to the movement of funds between defendants. They do not, in any event, render the assets unavailable for execution if the plaintiffs are successful at trial.

Conclusion

[57] For these reasons, the motion for a *Mareva* injunction is dismissed.

[58] I feel compelled to say a word about document production – in particular, financial and other records relating to transfers by, to, or between any of the party defendants. As noted earlier, this case will in large measure turn on an assessment of the source and destination of the Yorkville project's funds and whose money was being transferred, when, where and why. This will require careful and detailed forensic accounting evidence about the transfers in question. It is obvious, therefore, that full and immediate document production of all relevant transfers involving all the defendants will be critical to this exercise.

[59] There has been a suggestion that the defendants have been less than forthright in producing, or have refused to produce, financial records of some of the defendant entities. I do not know whether that is true; the question was not before me on this motion.

[60] What I want to emphasize is that the quality and extent of the evidence has been a material factor in my disposition of this motion. The quality and extent of the evidence, in particular

documentary evidence, will continue to be highly material as this matter progresses toward trial.

[61] I say all this to make one simple point. Prompt and comprehensive disclosure of the defendants' financial records is critically important. The defendants have virtually all the information relevant to this aspect of the case; the plaintiffs have almost none. Obviously, a party cannot produce a document that does not exist or which is not within the party's power, possession or control. Short of that, however, prompt and complete disclosure of all relevant financial information must be the operating principle at this stage of the proceedings. It is to be hoped that issues concerning document production in this case will not have to come before the court again.

Costs

[62] The parties have agreed that the successful party will be awarded all inclusive, partial indemnity costs of $94,497.62. It is so ordered.

Penny J.

Date: January 28, 2022

TAB 3

Court of Queen's Bench of Alberta

Citation: Alberta Energy Regulator v Lexin Resources Ltd, 2018 ABQB 590

Date: 20180808
Docket: 1701 03460
Registry: Calgary

Between:

Alberta Energy Regulator

Applicant

- and -

Lexin Resources Ltd., 1051393 B.C. Ltd., 0989 Resource Partnership, LR Processing Ltd., and LR Processing Partnership

Respondents

Decision
of the
Honourable Madam Justice B.E. Romaine

I. Introduction

[1] This is an application by the Receiver of Lexin Resources Ltd, 1051393 BC Ltd, 0989 Resource Partnership, LR Processing Ltd and LR Processing Partnership (the Lexin Group) seeking advice and direction respecting the characterization of funds indirectly advanced by MFC Energy Finance Inc to the 0989 partnership, a member of the Lexin Group, on June 30, 2015. The original amount of the advance was $37,570,500 (the Finance Advance). Finance advances a secured claim in the receivership against 0989 in the amount of $15,058,116.08, which it alleges is the remaining amount of the Finance Advance.

[2] For the reasons set out in this decision, I find that the Finance Advance is more properly characterized as equity rather than debt. In the alternative, I find that the Finance Advance should be postponed to the claims of other creditors pursuant to section 137 of *the Bankruptcy and Insolvency Act*, RSC 1985, C. B-3, as it is not a proper transaction.

II. Facts

[3] The relevant facts are as follows:

[4] MFC Bancorp Ltd (Bancorp) is a merchant banking company that invests in distressed businesses. In 2012, a subsidiary of Bancorp acquired the shares of Lexin Resources Inc, and in effect assumed or paid down Lexin's existing debt. At the time it did so, another of Bancorp's subsidiaries, MFC Energy Holding Austria Gmbh (MFC Austria) entered into two loan facility agreements with Austrian banks.

[5] Debt under these facilities was incurred in order to aid in the restructuring of Lexin, and used by the subsidiary to acquire a TD bank loan facility that had been used by Lexin's predecessor. The subsidiary and Lexin were then amalgamated, thus extinguishing Lexin's debt.

[6] While Finance submits that the intention was that the facility loans would be repaid from Lexin's cash flow, no loan agreement or other debt obligation has ever been put in place between MFC Austria and Lexin. Any payments by Lexin to MFC Austria have been made by way of a return of share capital.

[7] In 2013, Lexin's assets were transferred to the 0989 partnership, in which Lexin and Bancorp are partners. Again, there is no loan agreement between MFC Austria and 0989. The outstanding balance of the Finance Advance was reduced from time to time, and Finance now submits that the current balance is $15,058,116.08.

[8] In June, 2015, approximately $10.2 million in payments under the Austrian facilities became due.

[9] At this point in time, Bancorp held 100% of the shares of M Financial Corp (M Financial) and MFC Austria, which was wholly-owned by Bancorp, owned all the shares of Lexin. Lexin and Bancorp were partners of 0989, Lexin as to 66 2/3% and Bancorp as to 33.68%.

[10] Finance was incorporated on June 26, 2015 as a wholly-owned subsidiary of M Financial. Thus, each of Finance, M Financial, MFC Austria and Lexin were wholly –owned subsidiaries of Bancorp.

[11] Michael Smith was a director of Bancorp, M Financial, Finance, MFC Austria and Lexin and a member of the management committee of 0989.

[12] The following transactions all occurred on the same day, June 30, 2015:

(a) the directors of Finance resolved to issue 37,570,500 shares in Finance to M Financial for consideration of $37,570,500 and to grant a loan to 0989 in the same amount. Mr. Smith and Samuel Morrow, a director of Finance, MFC Austria and Bancorp, signed the directors' resolution. At the time, Finance had no other business or assets;
(b) 0989 received a wire transfer of $37,570,500 directly from M Financial;

[13] Finance and 0989 entered into a demand loan agreement dated June 30, 2015 which states that Finance was providing a loan to 0989 in the amount of $37,570,500. As security for the loan, 0989 and Lexin executed a general security agreement and 0989 executed a demand promissory note payable to Finance in the amount of the advance, all dated June 30, 2015. Before this, neither 0989 nor Lexin had any debt.

[14] All of the documentation with respect to the Finance Advance was signed or co-signed by Mr. Smith on behalf of both Finance and 0989.

[15] The loan agreement between Finance and 0989, provides, among other things, that:

(a) the Finance Advance is to be payable by 0989 only upon demand of Finance. There is no schedule for repayment;
(b) interest will only accrue if 0989 commits an event of default;
(c) 0989 is prohibited from selling assets of a value of more than $100,000 in any 12 month period, other than usual course sales of assets;
(d) 0989 may only make a payment on account of redemption or a distribution or return of capital if Finance consents to such a payment; and
(e) Finance is free to assign its rights and obligations under the agreement.

[16] Prior to the receivership of 0989 and Lexin, only two variable payments were made by 06989 to Finance, and no interest was ever charged.

[17] 0989 did not record receiving $37,570,500 in its accounting records in June, 2015 or any other date, but instead recorded an account payable of $37,570,500 to M Financial and a corresponding reduction in the share capital account of 0989 and Lexin.

[18] On the same day, June 30, 2015, the management committee of the 0989 partnership resolved to issue distributions to its two partners, Lexin and Bancorp, in the total amount of $37,570,500. At the time the Finance Advance was made, Finance was aware of this resolution.

[19] 0989's bank records show that on June 30, 2015, $12,653.744.40 was transferred to Bancorp and $24,916,755.60 was transferred to Lexin, resulting in no net change in 0989's bank accounts. Again on the same day, Lexin transferred the $24,916,755.60 to MFC Austria, resulting in no net change in Lexin's bank accounts. Given the over lapping nature of Finance and Lexin's directors, it is reasonable to infer that Finance was aware of these transfers.

[20] On June 30, 2015, MFC Austria paid down the Austrian bank facilities in the amount of $10,200,000 and transferred the remaining approximately $15,000,000 back to M Financial, the originator of the funds, as repayment for a 2013 loan made by the M Financial to MFC Austria.

[21] In summary, the Finance Advance was received by 0989, not from Finance but from M Financial directly, on June 30, 2015, and the whole advance was withdrawn from 0989's account on the same day and transferred to each of Lexin and Bancorp. Bancorp received and kept $12,653,744.40. On the same day, Lexin transferred the entirety of the amounts it had received to MFC Austria, MFC Austria then paid part of the amount to reduce bank debt and the rest, about $15 million, to M Financial, the originator of the funds for the Finance Advance. 0989 and Lexin only served as conduits though which the money flowed.

[22] In December, 2015, Finance transferred a portion of Lexin and 0989's assets to itself in partial settlement of the Finance Advance, at a time when Lexin's liabilities to creditors had started to accrue.

III. Position of the Parties

[23] Finance submits that the Finance Advance is a debt incurred for purposes of recapitalizing Lexin Resources Ltd. and 0989 with some additional "local" leverage to reduce their costs of capital.

[24] The Receiver, however, submits that, when considering the Finance Advance in light of all the surrounding circumstances at the time it was advanced, including the economic reality of 0989 and Lexin and the manner in which the advance was used, the Finance Advance should properly be characterized as an equity contribution made by Finance to 0989. Thus, the Receiver seeks an order declaring that 0989 is not indebted to Finance by reason of the Finance Advance, and that any claim that Finance has against 0989 or Lexin as a result of the Finance Advance is an "equity claim" as that term is defined under the *BIA*.

[25] In the alternative, if the Finance Advance is determined to be debt, the Receiver submits it is appropriate to postpone the Finance Advance to the claims of all of Lexin and 0989's other creditors pursuant to section 137 of the *BIA*, as an improper transaction between the debtors and a non-arm's length party. Further in the alternative, the Receiver submits that the Finance Advance should be postponed pursuant to the doctrine of equitable subordination.

IV. Preliminary Issues

A. Procedural Unfairness

[26] Finance complains that the Receiver has acted unfairly in this application, in that contrary to the procedural order, it not only addressed the validity of the Finance Advance, but also its priority. I do not agree that the Receiver was limited in its submissions on these issues by the procedural order or that issues of priory and equitable subordination do not fall within the broad issue of the reasons for the Receiver's denial of the claim, or that the Receiver was not clear in its reasons for its denial of the claim, which were set out in its letter of November 29, 2017. Without agreeing that there was any unfairness, however, I allowed Finance to tender a late affidavit, and a few additional days to respond to the Receiver's submissions on equitable subordination. Finance was also given the opportunity of filing a supplemental brief.

B. Brown v Dunn

[27] Finance submits that, as the Receiver did not comply with ***Brown v Dunn*** by questioning Mr. Morrow on whether it was Finance's intention to create an equity claim, his evidence that the intention was to re-leverage 0989 with some debt should be accepted as contradicted. However, as noted by the Receiver, in the absence of an arm's length relationship, it is not the stated intention of the parties that is determinative of the character of the advance, but rather all of the surrounding circumstances. I agree that the issue is whether the substance of the transaction is different from what the parties expressed it to be: ***Re U.S. Steel Ltd***, 2016 ONSC 569, upheld 2016 ONCA 662m at para 140.

V. Analysis

A. Should the Finance Advance be characterized as an investment of capital in 0989 by Finance or as a loan by Finance to 0989?

[28] If the Finance Advance is characterized as an equity contribution, Finance's secured claim will be subordinated to the claims of all other "creditors by the operation of s. 140.1 of the *BIA*, which states that a creditor is not entitled to a dividend in respect of an equity claim until all claims that are not equity claims have been satisfied".

1. Onus

[29] In the normal course in an insolvency, the onus is on a creditor to prove its claim.

[30] While Finance concedes that it has the "initial" burden to prove that the Finance Advance is a secured claim in the receivership, it submits that it does not have the burden of disproving that the Finance Advance is equity, or that it ought to be subordinated. By this, Finance means that, once it has proved that there is a contract, pursuant to which one person delivers money, and the other person agrees to repay the borrowed amount. Finance has met its burden and the onus proving that the advance is equity shifts to the Receiver. Finance relies in this respect on comments made by the Court in ***U.S Steel***.

[31] Those comments were made in context of a contest between competing creditors, and not an application by a receiver for advice and directions with respect to its findings on the validity of a claim. The Receiver has made its objections to the claim clear: the transaction bears the characteristics of a claim in equity and not in debt. Thus, the normal rule that the creditor bears the onus of establishing otherwise should apply. In any event, even if the burden shifts to the Receiver, the Receiver has met the burden in this case.

2. Analysis

[32] The issue of: supra particular claim is to be treated as debt or equity is a matter of statutory interpretation: ***supra*** at para 152.

[33] An "equity claim" is defined in the *BIA* as a claim that is in respect of an equity interest, including a claim for a return of capital or a contribution in respect of such a claim. An "equity interest" is defined as a share in the corporation, or another right to acquire a share in the corporation, other than one that is derived from a convertible debt. As noted by Wilton-Seigel, J. in ***U.S. Steel***, this type of situation can be distinguished from the situation in ***Canada Deposit Insurance Corp v Canadian Commercial Bank***, [1992] 3 SCR 558, where the transaction was arm's length.

[34] In ***U.S. Steel***, the Court held at para 155-156 that the definition of "equity claim" can extend to a contribution to capital by a sole shareholder unaccompanied by a further issuance of shares. Further, the reference to "a return of capital" need not be limited to a claim in respect of express contribution to capital, and a transaction can be a contribution of capital in substance even if it is expressed otherwise.

[35] Both the Receiver and Finance rely on the decision of U.S. Steel, as the Court in that case considered the specific circumstances of the characterization of the claim, such as this one, involving wholly-owned subsidiaries engaged in non-arm's length transaction.

[36] As noted at para 154 of ***U.S. Steel***:

> In the circumstances of a sole shareholder, there is no practical difference..... between a shareholding of a single share and a shareholding of multiple shares. Accordingly, for the purposes of the definition of an "equity claim", there should be no difference between a payment to a debtor company on account of the issuance of new shares and a payment to a debtor company by way of a contribution to capital in respect of the existing shares.

[37] Thus, as was the case in ***U.S. Steel***, the determination of whether Finance's claim is to be treated as debt or equity must address, not just the expressed intentions of the parties as reflected in the transaction documentation but also the manner in which the transaction was implemented and the economic reality of the surrounding circumstances. The form of the documentation is merely the "point of departure": ***supra*** at para 149.

[38] The issue in situations where the parties are not arm's length is not what the parties say they intended regarding the substance of the transaction but the "underlying substantive reality of the transaction": ***supra*** para 167. As actually implemented, is the substance of the transaction different from what was expressed in the transaction documentation?

[39] It is not as simple as submitted by Finance. The approach to characterization is not merely a narrow "rubber-stamping" of the form of transaction chosen by the sole shareholder: ***supra*** para 168.

[40] While the characterization of the claim must be analyzed at the date of advance, subsequent behavior, rather than subsequent stated intention, may be relevant if it illuminates the intentions of the parties at the date of advance although it cannot on its own justify a re-characterization of such advance: ***U.S. Steel*** at para 195; ***Canadian Deposit Insurance*** at para 52. The determination is not based on inequitable behaviour, but on the underlying substantive reality of the transaction.

[41] ***U.S. Steel*** sets out a helpful two-part test in to be followed in situations involving parent-subsidiary relationships at paras 186-190:

> (a) subjectively, did the alleged lender actually expect to be repaid the principle amount of the loan with interest out of the cashflows of the alleged borrower; and
> (b) objectively, was the expectation reasonable under the circumstances?

[42] The Court in ***U.S. Steel*** referred to various factors used by American courts to aid in determining appropriate characterization, including the following:

> (a) the names given to the instruments, if any, evidencing the indebtedness;
> (b) the presence or absence of a fixed maturity date and schedule of payments. The American cases suggest that the absence of a fixed maturity date and a fixed obligation to repay is an indication that the advances were capital contributions and not loans;
> (c) the presence or absence of a fixed rate of interest and interest payments. Again, it is suggested that the absence of a fixed rate of interest and interest payments is a strong indication that the advances were capital contributions rather than loans;
> (d) the source of repayments. If the expectation of repayment depends solely on the success of the borrower's business, the cases suggest that the transaction has the appearance of a capital contribution;

(e) the adequacy or inadequacy of capitalization. Thin or inadequate capitalization is strong evidence that the advances are capital contributions rather than loans;
(f) the identity of interest between the creditor and the shareholder. If shareholders make advances in proportion to their respective stock ownership, an equity contribution is indicated;
(g) the security, if any, for advances;
(h) the corporation's ability to obtain financing from outside lending institutions. When there is no evidence of other outside financing, some cases indicate that the fact no reasonable creditor would have acted in the same manner is strong evidence that the advances were capital contributions rather than loans;
(i) the extent to which the advances were subordinated to the claims of outside creditors;
(j) the extent to which the advances were used to acquire capital assets. The use of the advance to meet the daily operating needs for the corporation, rather than to purchase capital assets, is arguably indicative of bona fide indebtedness; and
(k) the presence or absence of a sinking fund to provide repayments.

[43] However, these and other factors are no more than an aid in determining substantive reality and should not be used in a "score-card" manner: supra para 181.

[44] However, the Receiver submits that these factors overwhelmingly point to the Finance Advance being in reality equity and not debt, particular factors b), c), e), f) and j).

[45] While there is formal documentation in this case, it does not include a schedule for repayment and there is no obligation to pay interest until default. Since it is characterized as a demand loan, there is no fixed maturity date. Thus, it would be possible, and in fact has been the case, that no demand for repayment has been made. Although there is evidence indicating the commencement of enforcement proceedings by various creditors, and thus default, Finance has issued no formal notice of default and no interest is alleged to be payable.

[46] Payments made under the Finance Advance were sporadic and the first payment made was in the form of an actual transfer of assets to Finance and its subsidiaries. Two variable cash repayments were made in 2016.

[47] It is relevant that the Finance Advance was not available for use by 0989 for daily operations or the acquisition of assets, but was immediately flowed through to its partners as distributions.

[48] It is also relevant that Bancorp was a guarantor of the Austrian bank debt, and that the transaction allowed that debt to be paid down, to the advantage of the parent company.

[49] The Receiver submits that this series of transactions was a plan to save the consolidated Bancorp enterprise at the expense of Lexin, 0989 and their stakeholders and, in effect, to secure ties to equity distributions for themselves against the Lexin Group's assets. Thus, it submits, referring back to the first part of the two-part test, there was no subjective intention for the Finance Advance to have ever been repaid.

[50] As noted at para 257 of ***U.S. Steel***:

> As a polar case, I accept that there may be circumstances in which a parent corporation is expectation from the outset is that it will sacrifice a subsidiary's profitability over the long-term for the benefit of the consolidated enterprise. In

> such circumstances, a court could find that the parent corporation had no intentions of causing the subsidiary to repay with interest any financing extended to the subsidiary or, more precisely, no expectation that the subsidiary would generate sufficient cash flow to enable it to make such payments based on the parent's anticipated business plan for it. In such circumstances, a court could also find that the entire amount of the financing extended by the parent corporation to the subsidiary was, in reality, an equity contribution.

[51] Finance submits that there are valid responses to all of these factors. It submits that the fact that the Finance Advance is a demand loan is responsive to the lack of maturity date. As noted in ***U.S. Steel*** ,a lack of maturity date and the absence of a schedule for the principal payment may only indicate the desire for flexibility to align payments of principal with 0989's economic performance against the back drop of a cyclical industry: ***supra*** at para 224.

[52] Despite submissions by both parties, I am unable on the basis of the evidence before me to determine whether undercapitalization is an issue.

[53] However, for Finance, the lack of any interest provision except on default is more problematic. Mr. Morrow alleges that withholding tax issues are the reasons for the advance being non-interest bearing. While there is nothing improper about this, this lacks of interest implies equity disguised as debt. Business choices on structure, while otherwise entirely proper, can have consequences for characterization.

[54] The Receiver submits that the restructuring of 0989 and Lexin as of June 30, 2015 with additional debt at a time when these entities had no debt does not make commercial sense. I accept the Receiver's view, particularly as none of the funds remained with 0989 or Lexin, and $15 million went full-circle back to M Financial, as Finance was clearly aware was the plan.

[55] Finance states that the commercial propose of the Finance Advance was (i) to fund the repayment of the MFC Austria loans, and (ii) to recapitalize Lexin and 0989 with some additional leverage, with one advantage being to add a "modest amount of local leverage to reduce Lexin and 0989's cost of capital".

[56] However, there was no debt obligation between MCF Austria and Lexin or 0989 at any point in time.

[57] In addition, the explanation that a modest amount of local leverage would reduce 0989 and Lexin's costs of capital is inconsistent with the fact that, as early as December, 2014, Bancorp was pursing the disposition of some of the Lexin properties. The commercially unusual aspects of the Finance Advance, including its nature as a demand loan, the fact that it was payable only upon default and that it included restrictions on redemption, distribution and return of capital without Finance's consent, could hardly be considered to be attractive to a prospective purchaser, even if the loan did not bear interest until default. If a cash and debt offer was more attractive to a purchaser, it could be negotiated at the time of the sale.

[58] However, I am not able to decide the issue of the credibility of Mr. Morrow's assertions with respect to Finance's subjective expectations despite these contradictory indicators without the benefit of viva voce evidence. Thus, given the circumstances in which this application was heard, I must accept that Finance has met the first part of the two-part test.

[59] However, was that expectation reasonable in the circumstances? The surrounding economic circumstances provide context to this question.

[60] While Finance asserts that the Austrian bank loans were intended to be repaid from Lexin's cash flow, in 2013, when the loans were made, Finance provided funds to MFC Austria to repay the principal and interest installments due under the loans, as neither 0989 nor Lexin generated sufficient returns to make equity distributions.

[61] In 2014, Lexin did make payments to MFC Austria, but it was by way of a return of capital. Finance states that MFC Austria used these funds to reduce the MFC Austria loans and to partially repay M Financial for the amounts it had advanced to MFC Austria in 2013.

[62] The funds distributed to Lexin and Bancorp by 0989 on June 30, 2015 are characterized by Finance as distributions to 0989's partners. The funds distributed by Lexin to MFC Austria the same day are characterized by Finance as a return of capital to Lexin's sole shareholder, MFC Austria, by way of a reduction of share capital pursuant to Section 74 of the British Columbia *Business Corporations Act*, SBC 2002 c 57. This raises the issue of why the flow-through of funds to 0989 was structured as a loan.

[63] Finance's answer is that the benefit of this leverage was in reducing 0989 and Lexin's cost of capital. However, Finance also submits that purpose of the loan was to facilitate a future sale.

[64] Finance's counsel included in its brief a hypothetical example that purported to demonstrate this increased saleability. However, the hypothetical example did not adequately take into account the effect of the Finance Loan. The Receiver revised the example, incorporating both the advance and actual data from the June 30, 2015 Lexin financial statements. This revision shows that the result would be the opposite of what Finance suggested would be increased saleability and that the advance would make a sale less attractive. As noted previously, the uncommon aspects of the debt would more likely make the existence of the Finance Advance a negative, rather than a positive, despite the lack of interest prior to default.

[65] Between July and September of 2015, the Bancorp board approved a plan to sell all of Lexin's assets, and in Bancorp's consolidated financial statements dated December 31, 2015, Bancorp referred to declining prices for oil and gas beginning in December 2014 and further declining by September 2015, leading to impairment assessments on its hydrocarbon properties in each of 2013 and 2014. In those financial statements, Bancorp indicates that on December 30th, 2015, it sold a 95 percent interest in certain hydrocarbon assets to a third party for nominal and contingent consideration, and that the contingent consideration was valued at nil.

[66] Even though the June 30, 2015 transactions occurred prior to these financial statements, and thus, some of these records are dated after the date of the Finance Advance, subsequent events are sometimes relevant to the extent they illuminate the intentions of the parties at the time of the advance. In this case, the subsequent events followed within weeks and months of the advance. In any event, Bancorp knew of declining commodity prices in 2013 and 2014, thus, it cannot have had any objectively reasonable expectation that 0989 would be able to pay the principle amount of the Finance Advance out of cashflow, even without interest.

[67] The Receiver submits that it is clear that 0989 and Lexin were underperforming at the time of the Finance Advance, but Mr. Morrow alleges that Lexin was profitable, and that he was not aware of any creditor that was outstanding as of June 30, 2015 or the rest of 2015 that was not paid in full. However, affidavits filed by the municipalities of Willow Creek and Vulcan indicate that Lexin had failed to pay property taxes levied by the counties since 2015, resulting in

liens and seizures beginning in November, 2015. Mr. Morrow also relied on the GLG reserve reports for the period, but failed to mention that the report assumes that the company would have to incur costs of development much higher than expected cash flowed in 2017 in order to earn such cash flows. The unaudited consolidated financial statements, without notes, do not aid in the determination of whether the expectation of repayment was objectively reasonable.

[68] In conclusion, I find that the expectation that the Finance Advance would be repaid by the borrower from cashflow was not objectively reasonable, and that the Finance Advance is properly characterized as an equity contribution.

[69] In the event I am wrong in this determination, I have considered whether it is appropriate to postpone the Finance Advance to all of Lexin and 0989's other creditors.

B. Should the Finance Advance be postponed pursuant to section 137 of the *BIA*?

[70] Section 137 of the *BIA* provides that a non-arm's length creditor that entered into a transaction with the debtor before bankruptcy is not entitled to payment of its claim arising from that transaction "until all claims of the other creditors have been satisfied, unless the transaction was in the opinion of the...court a proper transaction."

[71] It is clear that the Finance Advance was a transaction entered into with a non-arm's length party before bankruptcy. Thus, section 137 would postpone Finance's claim to the claims of other creditors unless this Court finds that the Finance Advance was a "proper transaction".

1. Onus

[72] When a debt claim is being advanced by a non-arm's length party, the claimant has the onus of proving that the transaction is a proper claim if it hopes to avoid having the claim subordinated pursuant to section 137 of the *BIA*: ***Re Tudor Sales Ltd***, 2017 BCSC 119 at para 48. However, even if I am wrong in this regard, the Receiver has satisfied the onus of establishing that the Finance Advance is not a proper transaction for the purpose of section 137.

2. Analysis

[73] Finance submits that, if the Finance Advance is debt, the Court cannot find that it is not a proper transaction under s. 137, relying on ***Stone Mountain Resource Holdings Ltd v Stone Mountain Resources Ltd***, 2012 ABQ 534. That is not what the Court in ***Stone Mountain*** establishes. Kent, J, found that the transaction in that case was for a proper purpose because a) there was no preference, and b) there was an injection of new money from an arm's length creditor to the debtor's parent company, and a subsequent loan of that money to the debtor subsidiary as a direct contribution to the debtor company's working capital, in accordance with a development plan: ***supra*** paras 31, 39-43.

[74] The facts in this case are different from those in ***Stone Mountain***. In this case, the funds advanced were flowed through 0989 as distributions to its partners, leaving 0989 without additional operating funds or working capital but only debt.

[75] In addition, there is nothing in the plain language of section 137 that would prevent it from applying to a transaction that is structured as debt. Indeed, the postponement created by the section would not be necessary if it applied merely to equity.

[76] The Receiver references ***Tudor Sales*** as a case that considered issues similar to the ones that arise here.

[77] In ***Tudor***, the applicant was an unsecured creditor of the bankrupt Tudor, seeking an order under section 135(5) of the *BIA* that the claim of a shareholder of Tudor with respect to shareholder loans be expunged or subordinated to the claims of other creditors.

[78] There was no written documentation of the shareholder loans, no fixed interest rate and no schedule for repayment. The advances were secured by a GSA. The interest rate that the company paid to the shareholder each year fluctuated with the fortunes of the company.

[79] The Court first considered whether the shareholder loans should be characterized a debt or equity, and found them to be equity, not because of the lack of a schedule for repayment or the absence of loan documentation, but because of the variable nature of the interest payments and the circumstances surrounding the advances at the time they were made. The Court considered events that took place shortly after the dates of the advances, noting that the "very close proximity in time" between the advances and these subsequent events "strongly implies that [the] advances were in substance consideration paid for [the shareholder's] ownership stake." Saunders, J. thus found the purported shareholder loans to be equity claims. The Court also considered whether the claim would fail by reason of section 137(1), and was satisfied that there was "simply no justification for allowing [the shareholder] the luxury of securing his investment in [another venture] through the mechanism of the GSA... and thereby defeating the legitimate interests of creditors": para 47.

[80] The Receiver submits that the Finance Advance was not made for the purpose of Lexin or 0989's ongoing operating expenses, or for their benefit at all, rather it was made for the sole purpose of enabling 0989 to issue partnership distributions which were ultimately return to Bancorp, MFC Austria and M Financial the originator of the funds, on the same day they were received.

[81] As previously noted, Finance claims that the purpose underlying the Finance Advance was to "recapitalize Lexin and 0989 with some additional leverage" and "reduce Lexin and 0989's costs of capital. This assertions is inconsistent with certain of Finance's other evidence, including the fact that at the time the Finance Advance was made, neither Lexin or 0989 had any debt. I accept that the substantive reality of the transactions was that, through the Finance Advance, Bancorp and its subsidiaries, including Finance, made equity distributions to themselves with their own funds, and secured such distributions against the assets of Lexin and 0989, both of whom previously had no debt.

[82] Mr. Morrow's evidence is that the purpose of the Finance Advance was to "facilitate a potential sale of the company at some point in the future through a deal that could include as part of the consideration an acquisitions of debt as opposed to a purely cash sale." Finance submits that this is evidence of a legitimate business purpose, and a benefit to 0989 and Lexin. As noted previously, a cash and debt sale could also be accomplished thought negotiation at the time of sale, and the hypothetical submitted through on Finances behalf does not support this theory.

[83] Finance also suggests that a benefit accrued to 0989 and Lexin in that MFC Austria used the proceeds of the MFC Austria loans to satisfy Lexin's pre-acquisition secured debt. However, 0989 and Lexin have no liability for that debt.

[84] Finance submits that, by retiring the debt, it freed up Lexin's cash flow but it is clear that in 2013 and 2014, cash flow was insufficient to warrant distributions sufficient to cover the Austrian loan. The Finance Advance occurred two and a half years after the alleged benefit, after

numerous inter-corporate distributions, and in a climate of acknowledged declines in commodity prices. I find that there was no appreciable benefit to 0989 and Lexin in imposing debt as part of the 2015 transactions.

[85] I agree that the purpose and result of the Finance Advance was to leverage 0989 and Lexin for the benefit of Bancorp, which was at risk as a guarantor of the MFC Austria loan, and to benefit MFC Austria.

[86] As noted in ***U.S. Steel*** at para 257, there may be circumstances in which a parent corporation will sacrifice a subsidiary's profitability over the long-term for the benefit of the consolidated enterprise. This is that type of case. It does not fall within the exception set out in section 37 as a proper transaction.

C. Should the Finance Advance be postponed pursuant to the doctrine of equitable subordination?

[87] It is not necessary in this case to resort to the doctrine of equitable subordination, given that I have found the Finance Advance to be in substance equity rather than debt, and, in the alternative, debt that must be subordinated claims of the other creditors under s. 137 of the *BIA*.

[88] Application of the doctrine by the courts in Canada has been inconsistent. Most recently, the Ontario Court of Appeal in ***Re U.S. Steel***, 2016 ONCA 662 declined to grant a declaration that the *CCAA* contains no restrictions within the meaning of s. 11 on the court's ability to apply the doctrine of equitable subordination, noting that "this is the wrong inquiry": para 100. The Court instead declined to grant the relief sought because there was no specific authority within the *CCAA* to apply the doctrine, and the appellant had not identified how the doctrine would further the remedial purpose of the *CCAA*: para 102.

[89] The Receiver describes the elements of the American doctrine in the terms set out by the Supreme Court in Canada in the 1992 case of ***Canada Deposit Insurance***. However, as noted in ***Re Blue Range Resource Corp***, 2000 ABQB 4 at para 50, and in ***Re I. Waxman & Sons Limited***, [2008] OJ No 885 at para 29, the doctrine as interpreted in American cases is not static, and appears to have evolved over time to the point that it no longer requires inequitable conduct by the creditors but rather depends on considerations of fairness on a case-by-case basis. This illustrates the danger of "taking a doctrine divorced from its legal home and applying it to Canada's statutory bankruptcy regime unencumbered with deep knowledge of the origin, development and legal system from which it originated": ***Waxman*** at para 33.

[90] At any rate, this case does not require consideration of the doctrine of equitable subordination; since the provisions set out in the *BIA* at sections 140.1and 137 are sufficient to determine the issue.

Dated at the City of Calgary, Alberta this 08th day of August, 2018.

B.E. Romaine
J.C.Q.B.A.

Appearances:

Robin Gurofksy and Jessica L. Cameron
for the Receiver Grant Thorton

Douglas A. McGillivray, Q.C., David LeGeyt and David A. de Groot
for MFC Energy Finance Inc.

Keely R. Cameron
for the Alberta Energy Regulator

Chris D. Simard
for Exxon Mobil Energy Canada

Gregory C. Plester and Megan Van Huizen
for the Municipal District of Willow Creek No. 26 and Vulcan County

Mary Buttery
for Energy Leasing Partners Ltd.

Richard Billington, Q.C.
for Young Energy Services Inc.

Karen Fellows
for MNP Ltd.

David Girard
for MD of Foothills Ranchland

TAB 4

COURT OF APPEAL

CANADA
PROVINCE OF QUEBEC
REGISTRY OF MONTREAL

No.: 500-09-029728-219
(700-11-020320-216)

DATE: October 11, 2022

CORAM: THE HONOURABLE MARTIN VAUCLAIR, J.A.
GENEVIÈVE MARCOTTE, J.A.
BENOÎT MOORE, J.A.

IN THE MATTER OF THE NOTICE OF INTENTION TO MAKE A PROPOSAL OF AZOXCO CRYOGÉNIQUE INC.:

ALAIN MASSE, in his capacity as trustee of FIDUCIE FAMILIALE ALAIN MASSE
VALÉRIE LACOMBE, in her capacity as trustee of FIDUCIE FAMILIALE ALAIN MASSE
APPELLANTS – Creditors

v.

AZOXCO CRYOGÉNIQUE INC.
RESPONDENT – Debtor

JUDGMENT

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[1] The appellants appeal against a judgment rendered by the Superior Court on October 1, 2021 (the Honourable Madam Justice Danielle Turcotte),[1] which annulled the decision of the respondent's trustee to allow their proof of claim as unsecured creditors, characterized said claim as an equity claim under s. 2 of the *Bankruptcy and Insolvency*

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1 *Avis d'intention de Azoxco Cryogénique inc.*, 2021 QCCS 4100 [judgment under appeal].

Act[2] ("*BIA*") and declared that the appellants are not entitled to vote on the respondent's proposal.

[2] The facts are as follows. On June 28, 2019, the appellants, who were shareholders of Azoxco Cryogénique Inc. ("Pre-amalgamation Azoxco") at the time, sold all of their shares to 9397-5530 Québec Inc. ("Québec Inc."). An amount of $2,535,000 was paid, with a balance payable at a later date.

[3] That same day, and as provided for in section 0.01.06 of the contract for the sale of shares, Québec Inc. and Pre-amalgamation Azoxco carried out a short-form amalgamation through which the first entity absorbed the second. The amalgamated corporation adopted the name Azoxco Cryogénique. The amalgamated corporation is the respondent, which therefore became the debtor for the balance of the share sale price.

[4] On August 25, 2020, the appellants, who had still not been paid, claimed from the respondent an amount of $1,952,817, representing the balance of the selling price. The respondent presented a defence and filed a cross-application, alleging fraud and misrepresentation by the appellants.

[5] In February 2021, the respondent filed a notice of intention to make a proposal to its creditors, which led to a stay of the appellants' proceedings. The stay was subsequently lifted.

[6] On February 2, 2021, the appellants filed a proof of claim as unsecured creditors.

[7] On July 8, 2021, the meeting of creditors was adjourned for the purpose of obtaining a legal opinion on the admissibility of the appellants' claim.

[8] On August 6, 2021, the trustee announced that it was accepting the appellants' claim.

[9] The effect of this decision would be to cause the respondent's bankruptcy because the appellants held the deciding vote and, unlike the other creditors, intended to vote against the proposal. The respondent therefore challenged the trustee's decision under s. 37 *BIA*. This is the issue that was adjudicated in the judgment under appeal.

[10] Based on s. 286 of the *Business Corporations Act*[3] ("*BCA*"), the judge concluded that the amalgamation had not changed the nature of the claim, as the rights and obligations of the amalgamating corporations had become those of the amalgamated corporation. The judge also noted that, in their pleadings, the appellants themselves

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2 R.S.C. (1985), c. B-3

3 CQLR, c. S-31.1.

had alleged that the claim was in respect of the balance of the selling price of the Pre-amalgamation Azoxco shares.

[11] Applying the principles developed by the Ontario Court of Appeal in *Sino-Forest*,[4] pursuant to which the notion of equity claim must be given an expansive interpretation and the analysis must focus on the nature of the claim rather than the identity of the claimant, the judge found that the appellants' claim was in respect of equity. Although the judge did not state it explicitly, she linked the claim to "a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest" set out in paragraph (d) of the definition.

* * *

[12] It will be helpful to reproduce certain provisions of the *BIA*:

2. […]	**2.** […]
equity interest means • **(a)** in the case of a corporation other than an income trust, a share in the corporation — or a warrant or option or another right to acquire a share in the corporation — other than one that is derived from a convertible debt, and • **(b)** in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt; (*intérêt relatif à des capitaux propres*)	***intérêt relatif à des capitaux propres*** • **a)** S'agissant d'une personne morale autre qu'une fiducie de revenu, action de celle-ci ou bon de souscription, option ou autre droit permettant d'acquérir une telle action et ne provenant pas de la conversion d'une dette convertible; • **b)** s'agissant d'une fiducie de revenu, part de celle-ci ou bon de souscription, option ou autre droit permettant d'acquérir une telle part et ne provenant pas de la conversion d'une dette convertible. (*equity interest*)
[…]	[…]
equity claim means a claim that is in respect of an equity interest, including a claim for, among others, • **(a)** a dividend or similar payment,	***réclamation relative à des capitaux propres*** Réclamation portant sur un intérêt relatif à des capitaux propres et visant notamment : • **a)** un dividende ou un paiement similaire;

[4] *Sino-Forest Corporation (Re)*, 2012 ONCA 816 [*Sino-Forest*].

- **(b)** a return of capital,
- **(c)** a redemption or retraction obligation,
- **(d)** a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
- **(e)** contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d); (*réclamation relative à des capitaux propres*)

- **b)** un remboursement de capital;
- **c)** tout droit de rachat d'actions au gré de l'actionnaire ou de remboursement anticipé d'actions au gré de l'émetteur;
- **d)** des pertes pécuniaires associées à la propriété, à l'achat ou à la vente d'un intérêt relatif à des capitaux propres ou à l'annulation de cet achat ou de cette vente;
- **e)** une contribution ou une indemnité relative à toute réclamation visée à l'un des alinéas a) à d). (*equity claim*)

[…]

54.1 Despite paragraphs 54(2)(a) and (b), creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise.

[…]

54.1 Malgré les alinéas 54(2)a) et b), les créanciers qui ont des réclamations relatives à des capitaux propres font partie d'une même catégorie de créanciers relativement à ces réclamations, sauf ordonnance contraire du tribunal, et ne peuvent à ce titre voter à aucune assemblée, sauf ordonnance contraire du tribunal.

[13] It will also be helpful to reproduce s. 286 *BCA*:

286. A certificate of amalgamation, issued by the enterprise registrar in accordance with Chapter XVIII, attests the amalgamation of the corporations as of the date and, if applicable, the time shown on the certificate.

As of that time, the amalgamating corporations are continued as one corporation and, as of that time, their patrimonies are joined together to form the patrimony of the amalgamated corporation. The rights and obligations of the amalgamating corporations become

286. Le certificat de fusion, délivré par le registraire des entreprises conformément aux dispositions du chapitre XVIII, atteste de la fusion des sociétés à la date et, le cas échéant, à l'heure figurant sur ce certificat.

À compter de ce moment, les sociétés fusionnantes continuent leur existence dans la société issue de la fusion et leurs patrimoines n'en forment alors qu'un seul qui est celui de la société issue de la fusion. Les droits et les obligations des

rights and obligations of the amalgamated corporation and the latter becomes a party to any judicial or administrative proceeding to which the amalgamating corporations were parties.	sociétés fusionnantes deviennent ceux de la société issue de la fusion et celle-ci devient partie à toute procédure judiciaire ou administrative à laquelle étaient parties les sociétés fusionnantes.

[14] It is necessary to clearly identify what is at issue in this appeal.

[15] A corporation's equity constitutes the shareholders' assets. It consists, in particular, of the issued and paid-up share capital or the retained earnings.[5]

[16] The rule set out in s. 54.1 *BIA*, which prohibits holders of equity claims from voting on a proposal, is intended, on the one hand, to prevent such holders from controlling the outcome of the vote and, on the other hand, to prioritize the protection of creditors who, unlike shareholders and other equity holders, have not participated in a speculative adventure.[6] Insolvency is a risk associated with the investment made by shareholders and, indeed, that risk justifies their potential profits. Author Frank Bennet has the following to say on this point:[7]

> **EQUITY CLAIMS**
>
> Claims against a company that result from ownership, purchase or sale of an equity interest in the debtor company and related indemnity claims are considered equity claims. Such claims as shareholders' claims can result in significant upside while creditors who supply goods and services do not share in the same upside. Consequently, there can be no distribution to holders of equity claims unless non-equity claimants are paid in full. Shareholders cannot expect to receive a dividend until all the creditors are satisfied. Shareholders do not have any financial interest in the debtor company until that happens.
>
> [Reference omitted]

[17] The definition of "equity claim" in s. 2 *BIA* includes, *among others*, a dividend, a redemption obligation, or a monetary loss resulting from the ownership, purchase or sale of an equity interest. The issue in the matter at hand, therefore, is whether the appellants' claim falls within this list, which, through the use of the words "among others", indicates that the list is not exhaustive.

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5 See: Raymonde Crête and Stéphane Rousseau, *Droit des sociétés par actions*, 4th ed., Montreal, Les Éditions Thémis, 2018, nos. 495 and 496.

6 *Royal Bank of Canada v. Central Capital Corp.*, 38 C.B.R. (3d) 1, 1996 CanLII 1521 (ON CA), para. 149.

7 Frank Bennett, *Bennett on Bankruptcy*, 24th ed., Toronto, LexisNexis, 2022, p. 1371. His comments pertain to the definition of "equity claim" under s. 2 of the *Companies' Creditors Arrangement Act*, R.S.C. (1985), c. C-36, which is identical to the definition in s. 2 *BIA*.

[18] The uniqueness of this case can be summarized as follows. Upon the sale of the shares, the appellants' claim against Québec Inc. was in respect of shares – thus equity – of Pre-amalgamation Azoxco, which was a third party to the contract. This means that, as between the parties to the contract, and pursuant to the *BIA*, the appellants had an unsecured claim against Québec Inc. It also means that at this point, if Pre-amalgamation Azoxco had become bankrupt, the appellants would not have had a claim or held equity with respect to it. The shares of Pre-amalgamation Azoxco held by Québec Inc. were an asset of Québec Inc.

[19] However, as a result of the amalgamation, the respondent, as the continuation of Québec Inc.'s juridical personality, assumed the debt owed by Québec Inc., and the shares of Pre-amalgamation Azoxco held by Québec Inc. were cancelled. Consequently, the issue is whether the claim, insofar as it is in respect of equity of one of the entities that resulted in the creation of the respondent, is a claim in respect of equity, within the meaning of s. 2 *BIA*, of the respondent. If it is, then, pursuant to s. 54.1 *BIA*, the appellants cannot vote on the proposal. If it is not, they can indeed vote.

[20] The appellants submit that the judge erred when, taking into account the amalgamation, she changed the nature of their claim against Québec Inc. – which was merely an unsecured claim – into an equity claim. In their view, the amalgamation could not have had that effect, because under s. 286 *BCA*, the amalgamation merely transferred Québec Inc.'s debt to the respondent, but did not modify that debt. It was an unsecured claim – which is not contested – and remained so.

[21] The appellants further argue that in order for their claim to be characterized as an equity claim, it was necessary that, at the time of the notice of intention, they hold a share in the respondent, or a warrant, an option or other analogous right. That said, not only was that not the case, but s. 282 *BCA* provides that the shares of Pre-amalgamation Azoxco, which the appellants sold, no longer existed and were not replaced by shares in the respondent. Therefore, the appellants were never shareholders of the respondent.

[22] As for the respondent, it argues that our Court owes great deference to the trial judge, both because she was seized of a question of mixed law and fact and because s. 37 *BIA* confers broad discretion on her. It further argues that the judge was correct in applying the analytical framework set out in *Sino-Forest*, in which the Ontario Court of Appeal established that the important factor is the nature of the claim, not the status of the claimant – that is, whether or not it is a shareholder.[8] In the respondent's view, applying the appellants' interpretation would depart from that principle by requiring that, at the moment the notice of intention is filed, the claimant hold a share or other type of equity interest. It would also indirectly achieve what s. 54.1 of the *BIA* seeks to proscribe, by allowing the appellants to vote on the proposal.

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[8] *Sino-Forest, supra,* note 4, para. 46.

[23] Before this Court, the parties both contend, as the trial judge did, that the amalgamation did not change the nature of the appellants' claim, but they draw contrary conclusions. The respondent, however, had argued the opposite in its motion appealing the trustee's decision. Upon reflection, and as explained below, whether or not the amalgamation changed the nature of the claim ultimately depends on the angle from which one analyzes the case.

[24] As stated above, at the time of the sale of the shares, the nature of the appellants' claim against their debtor, Québec Inc., was not in respect of the latter's equity, but rather the equity of a third party, namely Pre-amalgamation Azoxco. This means that if Québec Inc. had become bankrupt, the appellants could have filed a claim as unsecured creditors. This perspective supports the appellants' argument to the effect that by characterizing their claim as an "equity claim" after the amalgamation, the judge altered the nature of the initial claim and, in so doing, the appellants' insolvency risk.

[25] Conversely, the nature of the debt can also be viewed from the perspective of what was sold. In the present case, the appellants sold all the shares of Pre-amalgamation Azoxco, and a balance of sale was owed to them by Québec Inc. Their claim pertained to shares of Pre-amalgamation Azoxco and, consequently, it pertained to an equity interest in that corporation. Following the sale, Pre-amalgamation Azoxco and Québec Inc. carried out a short-form amalgamation and became the respondent. In reality, this type of amalgamation is but a reorganization of the amalgamating corporations' share capital.[9] As Professor Paul Martel points out, the amalgamated corporation is not a different entity from the amalgamating corporations, but rather their continuation, such that the amalgamated corporation holds all the property, rights and obligations of the original entities, without third-party rights having been affected by the amalgamation.[10] This is the essence of what is set out in the second paragraph of s. 286 *BCA*. The respondent, therefore, found itself with all the assets and liabilities of Pre-amalgamation Azoxco and Québec Inc. As for Pre-amalgamation Azoxco's equity, it was cancelled and, given the facts, converted into a debt owed by the respondent. The respondent was therefore now obliged to pay a debt related to equity of one of the amalgamating entities whose juridical personality it continued.

[26] How should the matter be resolved?

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9 André Morisset and Jean Turgeon, *Droit des sociétés par actions*, vol. 2, Toronto, LexisNexis, 1991 (loose-leaf sheets, update no. 248, June 2022), pp. 1620 and 1623.

10 Paul Martel, *La société par actions au Québec : les aspects juridiques*, Montreal, Wilson & Lafleur, 2021, nos. 33-129 and 33-130. See also, *Banque Royale du Canada c. Banque Canadienne Impériale de Commerce*, J.E. 2000-1041, 2000 CanLII 8607 (C.A.), paras. 27-28, citing *R. v. Black & Decker Manufacturing Co*., [1975] 1 S.C.R. 411, p. 417 and *Lebeuf c. Groupe SNC-Lavalin inc*., [1999] RJQ 385, 1999 CanLII 13644 (C.A.), pp. 23-24.

[27] In the case at bar, the Court does indeed owe great deference to the trial judge's findings, because she exercised a power under s. 37 *BIA*, which gave her wide discretion.[11]

[28] In addition to this first reason for deference, there is the nature of the issue the trial judge had before her. Contrary to the appellants' contention, this was not a pure question of law, but rather a mixed question. Indeed, the judge's characterization of the nature of the claim was not a purely technical exercise; it required her to consider the circumstances of the matter at hand in order to seek out the true nature of the transaction.[12] In the present case, the sale of the shares was inextricably linked to the amalgamation. Not only was the amalgamation provided for in the contract, but it occurred in its wake. This concomitance and the integration of the steps that took place provide a genuine indication of the nature of the transaction and the interests at stake. This approach is all the more necessary as it has been noted that distinguishing equity from unsecured claims may be difficult at times because corporations are finding new mechanisms that can narrow the gap between these two categories.[13]

[29] Let us look at the issue differently and assume that the shares the appellants held in Pre-amalgamation Azoxco had been repurchased by Pre-amalgamation Azoxco itself (rather than through Québec Inc.). Logically, and in accordance with a broad interpretation of the definition of equity claim,[14] such a transaction should have been characterized as a transaction under paragraph (d) of the definition, since the unpaid balance indeed constituted a loss resulting from "the ownership, purchase or sale of an equity interest […]". Accepting the appellants' position would circumvent the application of s. 54.1 *BIA* by allowing them to vote on the proposal, which would be directly contrary to the legislature's intent to subordinate the interests of holders of equity interests to those of creditors.

[30] Lastly, the Court cannot accept the appellants' argument that the definition of "equity claim" presupposes that, at the time of the notice of intention, they had to hold a share in the respondent, or a warrant, an option or other such right. Not only would adding such a condition run counter to the broad and liberal interpretation of this definition and depart from the legislature's intent to subordinate the protection of holders of an equity interest to that of creditors – as already discussed above – but the very wording of the definition does not suggest it. Indeed, paragraph (d) of the definition

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11 *Medcap Real Estate Holdings Inc. (Re)*, 2022 ONCA 318, para. 25; Lloyd W. Houlden, Geoffry B. Morawetz and Janis P. Sarra, *Bankruptcy and Insolvency Law of Canada*, 4th ed., Toronto, Thomson Reuters, 2009 (loose-leaf, updated August 2022), no. 2:128, pp. 2-183 and 2-184.

12 *Trakopolis SaaS Corp (2007996 Alberta Ltd) (Re)*, 2020 ABQB 643, para. 65.

13 INSOL International, *Update on Shareholder and Equity – Related Claims in Insolvency Proceedings*, October 2013, Technical Series Issue No. 28, p. 6.

14 *Sino-Forest, supra,* note 4, paras. 40-41, citing the Supreme Court on the use of the expression "in respect of": *CanadianOxy Chemicals Ltd. v. Canada (Attorney General)*, [1999] 1 S.C.R. 743, para. 16.

refers to a monetary loss resulting from, among other things, the *sale* of an equity interest. Consequently, once such equity has been sold, the seller is, by definition, no longer its owner. Nonetheless, its claim can still be characterized as an equity claim under paragraph (d) of the definition. There is no reason to conclude otherwise because the matter at hand involves a balance of sale.

[31] This was also the conclusion of the Ontario Court of Appeal in *Sino-Forest*. In that case, the shareholders had sued the accountants, who had failed to detect inaccuracies in the financial information provided by the corporation. The Ontario Court of Appeal, upholding the decision of Morawetz, J., concluded that this claim was included in the definition of "equity claim" even if the claimant did not hold, and had never held, such equity. That case, admittedly, is not identical to the one before us, because, ultimately, the beneficiaries of the claim were equity holders. Nevertheless, in both cases, an analysis of the nature of the claim rather than the nature of the claimant indicates that the claim is in respect of an equity interest.

[32] Absent a palpable and overriding error committed by the trial judge in characterizing the genuine nature of the claim, the appeal must be dismissed.

FOR THESE REASONS, THE COURT:

[33] **DISMISSES** the appeal, with legal costs.

MARTIN VAUCLAIR, J.A.

GENEVIÈVE MARCOTTE, J.A.

BENOÎT MOORE, J.A.

Mtre Bernard Gravel
Mtre Guillaume Hébert
SOCIÉTÉ D'AVOCATS DEXAR
For the appellants

Mtre François D. Gagnon
Mtre Kevin Mailloux
BORDEN LADNER GERVAIS
For the respondent

Date of hearing: September 22, 2022

TAB 5

Paul Housen *Appellant*

v.

Rural Municipality of Shellbrook No. 493 *Respondent*

INDEXED AS: HOUSEN *v.* NIKOLAISEN

Neutral citation: 2002 SCC 33.

File No.: 27826.

2001: October 2; 2002: March 28.

Present: McLachlin C.J. and L'Heureux-Dubé, Gonthier, Iacobucci, Major, Bastarache, Binnie, Arbour and LeBel JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR SASKATCHEWAN

Torts — Motor vehicles — Highways — Negligence — Liability of rural municipality for failing to post warning signs on local access road — Passenger sustaining injuries in motor vehicle accident on rural road — Trial judge apportioning part of liability to rural municipality — Whether Court of Appeal properly overturning trial judge's finding of negligence — The Rural Municipality Act, 1989, S.S. 1989-90, c. R-26.1, s. 192.

Municipal law — Negligence — Liability of rural municipality for failing to post warning signs on local access road — Passenger sustaining injuries in motor vehicle accident on rural road — Trial judge apportioning part of liability to rural municipality — Whether Court of Appeal properly overturning trial judge's finding of negligence — The Rural Municipality Act, 1989, S.S. 1989-90, c. R-26.1, s. 192.

Appeals — Courts — Standard of appellate review — Whether Court of Appeal properly overturning trial judge's finding of negligence — Standard of review for questions of mixed fact and law.

The appellant was a passenger in a vehicle operated by N on a rural road in the respondent municipality. N

Paul Housen *Appelant*

c.

Municipalité rurale de Shellbrook nº 493 *Intimée*

RÉPERTORIÉ : HOUSEN *c.* NIKOLAISEN

Référence neutre : 2002 CSC 33.

Nº du greffe : 27826.

2001 : 2 octobre; 2002 : 28 mars.

Présents : Le juge en chef McLachlin et les juges L'Heureux-Dubé, Gonthier, Iacobucci, Major, Bastarache, Binnie, Arbour et LeBel.

EN APPEL DE LA COUR D'APPEL DE LA SASKATCHEWAN

Délits civils — Véhicules automobiles — Routes — Négligence — Responsabilité d'une municipalité rurale qui omet d'installer des panneaux d'avertissement le long d'une voie d'accès locale — Blessures subies par un passager dans un accident automobile sur une route rurale — Responsabilité imputée en partie à la municipalité rurale par la juge de première instance — La Cour d'appel a-t-elle eu raison d'infirmer la décision de la juge de première instance concluant à la négligence de la municipalité rurale? — The Rural Municipality Act, 1989, S.S. 1989-90, ch. R-26.1, art. 192.

Droit municipal — Négligence — Responsabilité d'une municipalité rurale qui omet d'installer des panneaux d'avertissement le long d'une voie d'accès locale — Blessures subies par un passager dans un accident automobile sur une route rurale — Responsabilité imputée en partie à la municipalité rurale par la juge de première instance — La Cour d'appel a-t-elle eu raison d'infirmer la décision de la juge de première instance concluant à la négligence de la municipalité rurale? — The Rural Municipality Act, 1989, S.S. 1989-90, ch. R-26.1, art. 192.

Appels — Tribunaux judiciaires — Norme de contrôle applicable en appel — La Cour d'appel a-t-elle eu raison d'infirmer la décision de la juge de première instance concluant à la négligence de la municipalité rurale? — Norme de contrôle applicable à l'égard des questions mixtes de fait et de droit.

L'appelant était passager dans le véhicule conduit par N sur une route rurale située sur le territoire de la

failed to negotiate a sharp curve on the road and lost control of his vehicle. The appellant was rendered a quadriplegic as a result of the injuries he sustained in the accident. Damages were agreed upon prior to trial in the amount of $2.5 million, but at issue were the respective liabilities, if any, of the municipality, N and the appellant. On the day before the accident, N had attended a party at the T residence not far from the scene of the accident. He continued drinking through the night at another party where he met up with the appellant. The two men drove back to the T residence in the morning where N continued drinking until a couple of hours before he and the appellant drove off in N's truck. N was unfamiliar with the road, but had travelled on it three times in the 24 hours preceding the accident, on his way to and from the T residence. Visibility approaching the area of the accident was limited due to the radius of the curve and the uncleared brush growing up to the edge of the road. A light rain was falling as N turned onto the road from the T property. The truck fishtailed a few times before approaching the sharp curve where the accident occurred. Expert testimony revealed that N was travelling at a speed of between 53 and 65 km/hr when the vehicle entered the curved portion of the road, slightly above the speed at which the curve could be safely negotiated under the conditions prevalent at the time of the accident.

The road was maintained by the municipality and was categorized as a non-designated local access road. On such non-designated roads, the municipality makes the decision to post signs if it becomes aware of a hazard, or if there are several accidents at one spot. The municipality had not posted signs on any portion of the road. Between 1978 and 1987, three other accidents were reported in the area to the east of the site of the appellant's accident. The trial judge held that the appellant was 15 percent contributorily negligent in failing to take reasonable precautions for his own safety in accepting a ride from N, and apportioned the remaining joint and several liability 50 percent to N and 35 percent to the municipality. The Court of Appeal overturned the trial judge's finding that the municipality was negligent.

Held (Gonthier, Bastarache, Binnie and LeBel JJ. dissenting): The appeal should be allowed and the judgment of the trial judge restored.

municipalité intimée. N a été incapable de prendre un virage serré et il a perdu la maîtrise de son véhicule. L'appelant est devenu quadriplégique à la suite des blessures subies dans l'accident. Les parties ont convenu avant le procès du montant des dommages-intérêts, qui ont été fixés à 2,5 millions de dollars. La question en litige était celle de savoir si la municipalité, N et l'appelant étaient responsables et, dans l'affirmative, dans quelles proportions. Le jour qui a précédé l'accident, N avait assisté à une fête à la résidence des T, non loin de la scène de l'accident. Durant la nuit, il a continué de boire à une autre fête, où il a rencontré l'appelant. Le matin, les deux hommes sont retournés en automobile à la résidence des T, où N a continué de boire, cessant de le faire quelques heures avant de prendre la route dans sa camionnette en compagnie de l'appelant. N n'était pas familier avec le chemin en question, mais il l'avait emprunté à trois reprises au cours des 24 heures qui avaient précédé l'accident pour aller et venir de la résidence des T. À l'approche de l'endroit de l'accident, la distance de visibilité était réduite en raison du rayon de courbure du virage et de la présence de broussailles poussant jusqu'au bord du chemin Une faible pluie tombait lorsque N s'est engagé sur le chemin en quittant la résidence des T. L'arrière de la camionnette a zigzagué à plusieurs reprises avant que le véhicule n'arrive aux abords du virage serré où l'accident est survenu. Selon le témoignage d'un expert, N roulait à une vitesse se situant entre 53 et 65 km/h lorsque le véhicule s'est engagé dans la courbe, soit une vitesse légèrement supérieure à celle à laquelle le virage pouvait être pris en sécurité eu égard aux conditions qui existaient au moment de l'accident.

Le chemin, qui était entretenu par la municipalité, appartenait à la catégorie des voies d'accès locales non désignées. La municipalité installe des panneaux de signalisation sur ces chemins si elle constate l'existence d'un danger ou si plusieurs accidents se produisent au même endroit. Elle n'avait installé aucune signalisation le long de cette portion du chemin. On a signalé trois autres accidents survenus de 1978 à 1987 à l'est du lieu de l'accident dont a été victime l'appelant. La juge de première instance a estimé que l'appelant était responsable de négligence concourante dans une proportion de 15 p. 100, du fait qu'il avait omis de prendre des précautions raisonnables pour assurer sa propre sécurité en acceptant de monter à bord du véhicule de N, et elle a réparti le reste de la responsabilité solidairement entre N (50 p. 100) et la municipalité (35 p. 100). La Cour d'appel a infirmé la conclusion de la juge de première instance selon laquelle la municipalité avait été négligente.

Arrêt (les juges Gonthier, Bastarache, Binnie et LeBel sont dissidents) : Le pourvoi est accueilli et la décision de la juge de première instance est rétablie.

Per McLachlin C.J. and L'Heureux-Dubé, Iacobucci, Major and Arbour JJ.: Since an appeal is not a re-trial of a case, consideration must be given to the standard of review applicable to questions that arise on appeal. The standard of review on pure questions of law is one of correctness, and an appellate court is thus free to replace the opinion of the trial judge with its own. Appellate courts require a broad scope of review with respect to matters of law because their primary role is to delineate and refine legal rules and ensure their universal application.

The standard of review for findings of fact is such that they cannot be reversed unless the trial judge has made a "palpable and overriding error". A palpable error is one that is plainly seen. The reasons for deferring to a trial judge's findings of fact can be grouped into three basic principles. First, given the scarcity of judicial resources, setting limits on the scope of judicial review in turn limits the number, length and cost of appeals. Secondly, the principle of deference promotes the autonomy and integrity of the trial proceedings. Finally, this principle recognizes the expertise of trial judges and their advantageous position to make factual findings, owing to their extensive exposure to the evidence and the benefit of hearing the testimony *viva voce*. The same degree of deference must be paid to inferences of fact, since many of the reasons for showing deference to the factual findings of the trial judge apply equally to all factual conclusions. The standard of review for inferences of fact is not to verify that the inference can reasonably be supported by the findings of fact of the trial judge, but whether the trial judge made a palpable and overriding error in coming to a factual conclusion based on accepted facts, a stricter standard. Making a factual conclusion of any kind is inextricably linked with assigning weight to evidence, and thus attracts a deferential standard of review. If there is no palpable and overriding error with respect to the underlying facts that the trial judge relies on to draw the inference, then it is only where the inference-drawing process itself is palpably in error that an appellate court can interfere with the factual conclusion.

Le juge en chef McLachlin et les juges L'Heureux-Dubé, Iacobucci, Major et Arbour : Étant donné que l'appel ne constitue pas un nouveau procès, il faut se demander quelle est la norme de contrôle applicable en appel à l'égard des diverses questions que soulève le pourvoi. La norme de contrôle applicable aux pures questions de droit est celle de la décision correcte et, en conséquence, il est loisible aux cours d'appel de substituer leur opinion à celle des juges de première instance. Les cours d'appel ont besoin d'un large pouvoir de contrôle à l'égard des questions de droit pour être en mesure de s'acquitter de leur rôle premier, qui consiste à préciser et à raffiner les règles de droit et à veiller à leur application universelle.

Suivant la norme de contrôle applicable aux conclusions de fait, ces conclusions ne peuvent être infirmées que s'il est établi que le juge de première instance a commis une « erreur manifeste et dominante ». Une erreur manifeste est une erreur qui est évidente. Les diverses raisons justifiant la retenue à l'égard des conclusions de fait du juge de première instance peuvent être regroupées sous trois principes de base. Premièrement, vu la rareté des ressources dont disposent les tribunaux, le fait de limiter la portée du contrôle judiciaire a pour effet de réduire le nombre, la durée et le coût des appels. Deuxièmement, le respect du principe de la retenue envers les conclusions favorise l'autonomie et l'intégrité du procès. Enfin, ce principe permet de reconnaître l'expertise du juge de première instance et la position avantageuse dans laquelle il se trouve pour tirer des conclusions de fait, étant donné qu'il a l'occasion d'examiner la preuve en profondeur et d'entendre les témoignages de vive voix. Il faut faire preuve du même degré de retenue envers les inférences de fait, car nombre de raisons justifiant de faire preuve de retenue à l'égard des constatations de fait du juge de première instance valent autant pour toutes ses conclusions factuelles. La norme de contrôle ne consiste pas à vérifier si l'inférence peut être raisonnablement étayée par les conclusions de fait du juge de première instance, mais plutôt si ce dernier a commis une erreur manifeste et dominante en tirant une conclusion factuelle sur la base de faits admis, ce qui suppose l'application d'une norme plus stricte. Une conclusion factuelle — quelle que soit sa nature — exige nécessairement qu'on attribue un certain poids à un élément de preuve et, de ce fait, commande l'application d'une norme de contrôle empreinte de retenue. Si aucune erreur manifeste et dominante n'est décelée en ce qui concerne les faits sur lesquels repose l'inférence du juge de première instance, ce n'est que lorsque le processus inférentiel lui-même est manifestement erroné que la cour d'appel peut modifier la conclusion factuelle.

Questions of mixed fact and law involve the application of a legal standard to a set of facts. Where the question of mixed fact and law at issue is a finding of negligence, it should be deferred to by appellate courts, in the absence of a legal or palpable and overriding error. Requiring a standard of "palpable and overriding error" for findings of negligence made by either a trial judge or a jury reinforces the proper relationship between the appellate and trial court levels and accords with the established standard of review applicable to a finding of negligence by a jury. Where the issue on appeal involves the trial judge's interpretation of the evidence as a whole, it should not be overturned absent palpable and overriding error. A determination of whether or not the standard of care was met by the defendant involves the application of a legal standard to a set of facts, a question of mixed fact and law, and is thus subject to a standard of palpable and overriding error, unless it is clear that the trial judge made some extricable error in principle with respect to the characterization of the standard or its application, in which case the error may amount to an error of law, subject to a standard of correctness.

Here, the municipality's standard of care was to maintain the road in such a reasonable state of repair that those requiring to use it could, exercising ordinary care, travel upon it with safety. The trial judge applied the correct test in determining that the municipality did not meet this standard of care, and her decision should not be overturned absent palpable and overriding error. The trial judge kept the conduct of the ordinary motorist in mind because she stated the correct test at the outset, and discussed implicitly and explicitly the conduct of a reasonable motorist approaching the curve. Further, her apportionment of negligence indicates that she assessed N's conduct against the standard of the ordinary driver as does her use of the term "hidden hazard" and her consideration of the speed at which motorists should have approached the curve.

The Court of Appeal's finding of a palpable and overriding error by the trial judge was based on the erroneous presumption that she accepted 80km/h as the speed at which an ordinary motorist would approach the curve, when in fact she found that a motorist exercising

Les questions mixtes de fait et de droit supposent l'application d'une norme juridique à un ensemble de faits. Lorsque la question mixte de fait et de droit en litige est une conclusion de négligence, il y a lieu de faire preuve de retenue à l'égard de cette conclusion en l'absence d'erreur de droit ou d'erreur manifeste et dominante. Le fait d'exiger l'application de la norme de l'« erreur manifeste et dominante » aux fins de contrôle d'une conclusion de négligence tirée par un juge ou un jury consolide les rapports qui doivent exister entre les juridictions d'appel et celles de première instance et respecte la norme de contrôle bien établie qui s'applique aux conclusions de négligence tirées par les jurys. Si la question litigieuse en appel soulève l'interprétation de l'ensemble de la preuve par le juge de première instance, cette interprétation ne doit pas être infirmée en l'absence d'erreur manifeste et dominante. La question de savoir si le défendeur a respecté la norme de diligence suppose l'application d'une norme juridique à un ensemble de faits, ce qui en fait une question mixte de fait et de droit. Cette question est alors assujettie à la norme de l'erreur manifeste et dominante, à moins que le juge de première instance n'ait clairement commis une erreur de principe en déterminant la norme applicable ou en appliquant cette norme, auquel cas l'erreur peut constituer une erreur de droit, qui est assujettie à la norme de la décision correcte.

En l'espèce, la norme de diligence à laquelle devait se conformer la municipalité consistait à tenir le chemin dans un état raisonnable d'entretien, de façon que ceux qui devaient l'emprunter puissent, en prenant des précautions normales, y circuler en sécurité. La juge de première instance a appliqué le bon critère juridique en concluant que la municipalité n'avait pas respecté cette norme et sa décision ne devrait pas être infirmée en l'absence d'erreur manifeste et dominante. La juge de première instance a eu à l'esprit la conduite de l'automobiliste moyen puisqu'elle a commencé son examen de la norme de diligence en formulant dès le départ le critère approprié, puis elle s'est interrogée, tant explicitement qu'implicitement, sur la façon dont conduirait l'automobiliste raisonnable en s'approchant du virage. De plus, le fait qu'elle a imputé une partie de la responsabilité à N indique qu'elle a évalué sa conduite au regard du critère du conducteur moyen, tout comme l'indique le fait qu'elle a utilisé l'expression « danger caché » et qu'elle s'est demandé à quelle vitesse les automobilistes auraient dû approcher du virage.

La conclusion de la Cour d'appel portant que la juge de première instance avait commis une erreur manifeste et dominante reposait sur la présomption erronée selon laquelle la juge aurait accepté que l'automobiliste moyen approcherait du virage à 80 km/h, alors que dans les faits

ordinary care could approach the curve at greater than the speed at which it would be safe to negotiate it. This finding was based on the trial judge's reasonable and practical assessment of the evidence as a whole, and is far from reaching the level of palpable and overriding error.

The trial judge did not err in finding that the municipality knew or ought to have known of the disrepair of the road. Because the hazard in this case was a permanent feature of the road, it was open to the trial judge to draw the inference that a prudent municipal councillor ought to be aware of it. Once this inference has been drawn, then unless the municipality can rebut the inference by showing that it took reasonable steps to prevent such a hazard from continuing, the inference will be left undisturbed. Prior accidents on the road do not provide a direct basis for finding that the municipality had knowledge of the particular hazard, but this factor, together with knowledge of the type of drivers using this road, should have caused the municipality to investigate the road which would have resulted in actual knowledge. To require the plaintiff to provide concrete proof of the municipality's knowledge of the state of disrepair of its roads is to set an impossibly high burden on the plaintiff. Such information was within the particular sphere of knowledge of the municipality, and it was reasonable for the trial judge to draw an inference of knowledge from her finding that there was an ongoing state of disrepair.

The trial judge's conclusion on the cause of the accident was a finding of fact subject to the palpable and overriding error standard of review. The abstract nature of the inquiry as to whether N would have seen a sign had one been posted before the curve supports deference to the factual findings of the trial judge. The trial judge's factual findings on causation were reasonable and thus should not have been interfered with by the Court of Appeal.

Per Gonthier, Bastarache, Binnie and LeBel JJ. (dissenting): A trial judge's findings of fact will not be overturned absent palpable and overriding error principally in recognition that only the trial judge observes witnesses and hears testimony first hand and is therefore better able to choose between competing versions of events. The process of fact-finding involves

elle a estimé qu'il était possible qu'un automobiliste prenant des précautions normales s'approche du virage à une vitesse supérieure à la vitesse sécuritaire pour effectuer la manœuvre. Loin de constituer une erreur manifeste et dominante, cette conclusion découlait d'une évaluation raisonnable et réaliste de l'ensemble de la preuve par la juge de première instance.

La juge de première instance n'a pas commis d'erreur en concluant que la municipalité connaissait ou aurait dû connaître le mauvais état du chemin. Étant donné que, en l'espèce, le danger était une caractéristique permanente du chemin, il était loisible à la juge de première instance d'inférer que le conseiller municipal prudent aurait dû être au fait du danger. Dès l'instant où une telle inférence est tirée, elle demeure inchangée à moins que la municipalité ne puisse la réfuter en démontrant qu'elle a pris des mesures raisonnables pour faire cesser le danger. Les accidents survenus antérieurement sur le chemin ne constituent pas une preuve directe permettant de conclure que la municipalité connaissait l'existence du danger particulier en cause, mais ce facteur, conjugué à la connaissance du type de conducteurs utilisant le chemin, aurait dû inciter la municipalité à faire enquête à l'égard du chemin en question, ce qui lui aurait permis de prendre connaissance concrètement de l'existence du danger. Exiger du demandeur qu'il apporte la preuve concrète de la connaissance par la municipalité du mauvais état d'entretien de ses chemins revient à imposer à ce dernier un fardeau inacceptablement lourd. Il s'agit d'information relevant du domaine de connaissance de la municipalité et, selon nous, il était raisonnable que la juge de première instance infère de sa conclusion relative au mauvais état d'entretien persistant du chemin que la municipalité possédait la connaissance requise.

La conclusion de la juge de première instance quant à la cause de l'accident était une conclusion de fait assujettie à la norme de contrôle de l'« erreur manifeste et dominante ». Le caractère théorique de l'analyse de la question de savoir si N aurait aperçu un panneau de signalisation installé avant la courbe justifie de faire montre de retenue à l'égard des conclusions factuelles de la juge de première instance. Les constatations factuelles de cette dernière relativement à la causalité étaient raisonnables et la Cour d'appel n'aurait donc pas dû les modifier.

Les juges Gonthier, Bastarache, Binnie et LeBel (dissidents) : Les conclusions de fait du juge de première instance ne sont pas modifiées en l'absence d'erreur manifeste ou dominante, principalement parce qu'il est le seul à avoir l'occasion d'observer les témoins et d'entendre les témoignages de vive voix, et qu'il est, de ce fait, plus à même de choisir entre deux versions

not only the determination of the factual nexus of the case but also requires the judge to draw inferences from facts. Although the standard of review is identical for both findings of fact and inferences of fact, an analytical distinction must be drawn between the two. Inferences can be rejected for reasons other than that the inference-drawing process is deficient. An inference can be clearly wrong where the factual basis upon which it relies is deficient or where the legal standard to which the facts are applied is misconstrued. The question of whether the conduct of the defendant has met the appropriate standard of care in the law of negligence is a question of mixed fact and law. Once the facts have been established, the determination of whether or not the standard of care was met will in most cases be reviewable on a standard of correctness since the trial judge must appreciate the facts within the context of the appropriate standard of care, a question of law within the purview of both the trial and appellate courts.

A question of mixed fact and law in this case was whether the municipality knew or should have known of the alleged danger. The trial judge must approach this question having regard to the duties of the ordinary, reasonable and prudent municipal councillor. Even if the trial judge correctly identifies this as the applicable legal standard, he or she may still err in assessing the facts through the lens of that legal standard, a process which invokes a policy-making component. For example, the trial judge must consider whether the fact that accidents had previously occurred on different portions of the road would alert the ordinary, reasonable and prudent municipal councillor to the existence of a hazard. The trial judge must also consider whether the councillor would have been alerted to the previous accident by an accident-reporting system, a normative issue reviewable on a standard of correctness. Not all matters of mixed fact and law are reviewable according to the standard of correctness, but neither should they be accorded deference in every case.

Section 192 of the *Rural Municipality Act, 1989*, requires the trial judge to examine whether the portion of the road on which the accident occurred posed a hazard to the reasonable driver exercising ordinary care. Here, the trial judge failed to ask whether a reasonable driver exercising ordinary care would have been able to safely drive the portion of the road on which the accident

divergentes d'un même événement. Le processus de constatation des faits exige non seulement du juge qu'il dégage le nœud factuel de l'affaire, mais également qu'il tire des inférences des faits. Bien que la norme de contrôle soit la même et pour les conclusions de fait et pour les inférences de fait, il importe néanmoins de faire une distinction analytique entre les deux. Des inférences peuvent être rejetées pour d'autres raisons que le fait que le processus qui les a produites est lui-même déficient. Une inférence peut être manifestement erronée si ses assises factuelles présentent des lacunes ou si la norme juridique appliquée aux faits est mal interprétée. Dans le contexte du droit relatif à la négligence, la question de savoir si la conduite du défendeur est conforme à la norme de diligence appropriée est une question mixte de fait et de droit. Une fois les faits établis, la décision touchant la question de savoir si le défendeur a respecté ou non la norme de diligence est, dans la plupart des cas, contrôlable selon la norme de la décision correcte, puisque le juge de première instance doit apprécier les faits au regard de la norme de diligence appropriée, question de droit qui relève autant des cours de première instance que des cours d'appel.

En l'espèce, la question de savoir si la municipalité connaissait ou aurait dû connaître le danger dont on alléguait l'existence était une question mixte de fait et de droit. Le juge de première instance doit examiner cette question eu égard aux obligations qui incombent au conseiller municipal moyen, raisonnable et prudent. Même en supposant que le juge de première instance détermine correctement la norme juridique applicable, il lui est encore possible de commettre une erreur lorsqu'il apprécie les faits à la lumière de cette norme juridique, processus qui implique notamment l'établissement de politiques d'intérêt général. Par exemple, il doit se demander si le fait que des accidents se soient déjà produits à d'autres endroits du chemin alerterait le conseiller municipal moyen, raisonnable et prudent de l'existence d'un danger. Il doit également se demander si ce conseiller aurait appris l'existence de l'accident antérieur par un système d'information sur les accidents, question normative qui est contrôlable selon la norme de la décision correcte. Les questions mixtes de fait et de droit ne sont pas toutes contrôlables suivant cette norme, mais elles ne commandent pas systématiquement une attitude empreinte de retenue.

Suivant la norme de diligence énoncée à l'art. 192 de la *Rural Municipality Act, 1989*, la juge de première instance devait se demander si le tronçon du chemin sur lequel s'est produit l'accident constituait un danger pour le conducteur raisonnable prenant des précautions normales. En l'espèce, la juge de première instance a omis de se demander si un tel conducteur aurait pu rouler

occurred. This amounted to an error of law. The duty of the municipality is to keep the road in such a reasonable state of repair that those required to use it may, exercising ordinary care, travel upon it with safety. The duty is a limited one as the municipality is not an insurer of travellers using its streets. Although the trial judge found that the portion of the road where the accident occurred presented drivers with a hidden hazard, there is nothing to indicate that she considered whether or not that portion of the road would pose a risk to the reasonable driver exercising ordinary care. Where an error of law has been found, the appellate court has jurisdiction to take the factual findings of the trial judge as they are and to reassess these findings in the context of the appropriate legal test. Here, the portion of the road on which the accident occurred did not pose a risk to a reasonable driver exercising ordinary care because the condition of the road in general signalled to the reasonable driver that caution was needed.

The trial judge made both errors of law and palpable and overriding errors of fact in determining that the municipality should have known of the alleged state of disrepair. She made no finding that the municipality had actual knowledge of the alleged state of disrepair, but rather imputed knowledge to it on the basis that it should have known of the danger. As a matter of law, the trial judge must approach the question of whether knowledge should be imputed to the municipality with regard to the duties of the ordinary, reasonable and prudent municipal councillor. The question is then answered through the trial judge's assessment of the facts of the case. The trial judge erred in law by approaching the question of knowledge from the perspective of an expert rather than from that of a prudent municipal councillor and by failing to appreciate that the onus of proving that the municipality knew or should have known of the disrepair remained on the plaintiff throughout. She made palpable and overriding errors in fact by drawing the unreasonable inference that the municipality should have known that the portion of the road on which the accident occurred was dangerous from evidence that accidents had occurred on other parts of the road. As the municipality had not received any complaints from motorists respecting the absence of signs on the road, the lack of super-elevation on the curves, or the presence of vegetation along the sides of the road, it had no particular reason to inspect that segment of the road for the presence of hazards. The question of the municipality's knowledge is inextricably linked to the standard of care. A municipality can only be expected to have knowledge of those hazards which pose a risk to the reasonable driver exercising ordinary care, since these are the only hazards for which there is

en sécurité sur le tronçon en question. Il s'agissait d'une erreur de droit. Les municipalités ont l'obligation de tenir les chemins dans un état raisonnable d'entretien de façon que ceux qui doivent les emprunter puissent, en prenant des précautions normales, y circuler en sécurité. Il s'agit d'une obligation de portée limitée, car les municipalités ne sont pas les assureurs des automobilistes qui roulent dans leurs rues. Bien que la juge de première instance ait conclu que la portion du chemin où s'est produit l'accident exposait les conducteurs à un danger caché, il n'y a rien qui indique qu'elle s'est demandé si cette portion du chemin présentait un risque pour le conducteur raisonnable prenant des précautions normales. La cour d'appel qui décèle une erreur de droit a compétence pour reprendre telles quelles les conclusions de fait du juge de première instance et les réévaluer au regard du critère juridique approprié. En l'espèce, la portion du chemin où s'est produit l'accident ne présentait pas de risque pour un conducteur raisonnable prenant des précautions normales, car l'état de ce chemin en général avertissait l'automobiliste raisonnable que la prudence s'imposait.

La juge de première instance a commis et des erreurs de droit et des erreurs de fait manifestes et dominantes en statuant que la municipalité intimée aurait dû connaître le mauvais état dans lequel se trouvait, prétendait-on, le chemin. La juge de première instance n'a pas conclu que la municipalité intimée connaissait concrètement le prétendu mauvais état du chemin, mais elle lui a plutôt prêté cette connaissance pour le motif qu'elle aurait dû connaître l'existence du danger. Sur le plan juridique, le juge de première instance doit se demander s'il y a lieu de présumer que la municipalité connaissait ce fait, eu égard aux obligations qui incombent au conseiller municipal moyen, raisonnable et prudent. Il répond ensuite à cette question en appréciant les faits de l'espèce dont il est saisi. Dans la présente affaire, la juge de première instance a fait erreur en droit en examinant la question de la connaissance requise du point de vue du spécialiste plutôt que du point de vue du conseiller municipal prudent et en ne reconnaissant pas que le fardeau de prouver que la municipalité connaissait ou aurait dû connaître le mauvais état du chemin ne cessait jamais d'incomber au demandeur. La juge de première instance a commis une erreur de fait manifeste et dominante en inférant déraisonnablement que la municipalité intimée aurait dû savoir que la partie du chemin où l'accident s'est produit était dangereuse, compte tenu de la preuve que des accidents avaient eu lieu ailleurs sur ce chemin. La municipalité n'avait aucune raison particulière d'aller inspecter cette portion du chemin pour voir s'il y existait des dangers, puisqu'elle n'avait reçu aucune plainte d'automobilistes relativement à l'absence de signalisation, à l'absence de surélévation des courbes ou à la présence d'arbres et de végétation en bordure du

a duty to repair. Here, the municipality cannot have been expected to have knowledge of the hazard that existed at the site of the accident, since the hazard did not pose a risk to the reasonable driver. Implicit in the trial judge's reasons was the expectation that the municipality should have known about the accidents through an accident reporting system, a palpable error, absent any evidence of what might have been a reasonable system.

With respect to her conclusions on causation, which are conclusions on matters of fact, the trial judge ignored evidence that N had swerved on the first curve he negotiated prior to the accident, and that he had driven on the road three times in the 18 to 20 hours preceding the accident. She further ignored the significance of the testimony of the forensic alcohol specialist which pointed overwhelmingly to alcohol as the causal factor which led to the accident, and erroneously relied on one statement by him to support her conclusion that a driver at N's level of impairment would have reacted to a warning sign. The finding that the outcome would have been different had N been forewarned of the curve ignores the fact that he already knew the curve was there. The fact that the trial judge referred to some evidence to support her findings on causation does not insulate them from review by this Court. An appellate court is entitled to assess whether or not it was clearly wrong for the trial judge to rely on some evidence when other evidence points overwhelmingly to the opposite conclusion.

Whatever the approach to the issue of the duty of care, it is only reasonable to expect a municipality to foresee accidents which occur as a result of the conditions of the road, and not, as in this case, as a result of the condition of the driver. To expand the repair obligation of municipalities to require them to take into account the actions of unreasonable or careless drivers when discharging this duty would signify a drastic and unworkable change to the current standard.

chemin. La question de la connaissance de l'intimée est intimement liée à celle de la norme de diligence. Une municipalité est uniquement censée avoir connaissance des dangers qui présentent un risque pour le conducteur raisonnable prenant des précautions normales, puisqu'il s'agit des seuls dangers à l'égard desquels existe une obligation d'entretien. En l'espèce, on ne pouvait attendre de l'intimée qu'elle connaisse le danger qui existait à l'endroit où l'accident est survenu, puisque ce danger ne présentait tout simplement pas de risque pour le conducteur raisonnable. Il ressort implicitement des motifs de la juge de première instance que la municipalité aurait censément dû connaître l'existence des accidents grâce à un système d'information en la matière, erreur manifeste en l'absence de quelque élément de preuve indiquant ce qui aurait pu constituer un système raisonnable.

Relativement aux conclusions de la juge de première instance sur le lien de causalité, qui sont des conclusions de fait, celle-ci a fait abstraction de la preuve que le véhicule de N avait fait une embardée dans la première courbe et que ce dernier avait roulé à trois reprises sur le chemin en question au cours des 18 à 20 heures ayant précédé l'accident. La juge de première instance a également omis de tenir compte de l'importance du témoignage du spécialiste judiciaire en matière d'alcool, qui menait irrésistiblement à la conclusion que l'alcool avait été le facteur causal de l'accident, et elle a erronément invoqué une déclaration de celui-ci au soutien de sa conclusion que N aurait réagi à un panneau de signalisation. La conclusion que le résultat aurait été différent si N avait été prévenu de l'existence de la courbe ne tient pas compte du fait qu'il savait déjà qu'elle existait. Le fait que la juge de première instance ait mentionné certains éléments de preuve au soutien de ses conclusions sur le lien de causalité n'a pas pour effet de soustraire ces conclusions au pouvoir de contrôle de notre Cour. Le tribunal d'appel est habilité à se demander si le juge de première instance a clairement fait erreur en décidant comme il l'a fait sur le fondement de certains éléments de preuve alors que d'autres éléments mènent irrésistiblement à la conclusion inverse.

Indépendamment de l'approche choisie à l'égard de la question de l'obligation de diligence, il n'est que raisonnable d'attendre d'une municipalité qu'elle prévoit les accidents qui surviennent en raison de l'état du chemin, et non, comme en l'espèce, ceux qui résultent de l'état du conducteur. Élargir l'obligation d'entretien des municipalités en exigeant qu'elles tiennent compte, dans l'exécution de cette obligation, des actes des conducteurs déraisonnables ou imprudents, entraînerait une modification radicale et irréalisable de la norme actuelle.

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Gary D. Young, *Q.C.*, *Denis I. Quon* and *M. Kim Anderson*, for the appellant.

Michael Morris and *G. L. Gerrand*, *Q.C.*, for the respondent.

The judgment of McLachlin C.J. and L'Heureux-Dubé, Iacobucci, Major and Arbour JJ. was delivered by

IACOBUCCI AND MAJOR JJ. —

I. Introduction

A proposition that should be unnecessary to state is that a court of appeal should not interfere with a trial judge's reasons unless there is a palpable and overriding error. The same proposition is sometimes stated as prohibiting an appellate court from reviewing a trial judge's decision if there was some evidence upon which he or she could have relied to reach that conclusion.

Authority for this abounds particularly in appellate courts in Canada and abroad (see *Gottardo Properties (Dome) Inc. v. Toronto (City)* (1998), 162 D.L.R. (4th) 574 (Ont. C.A.); *Schwartz v. Canada*, [1996] 1 S.C.R. 254; *Toneguzzo-Norvell (Guardian ad litem of) v. Burnaby Hospital*, [1994] 1 S.C.R. 114; *Van de Perre v. Edwards*, [2001] 2 S.C.R. 1014, 2001 SCC 60). In addition scholars, national and international, endorse it (see C. A. Wright in "The Doubtful Omniscience of Appellate Courts" (1957), 41 *Minn. L. Rev.* 751, at p. 780; and the Honourable R. P. Kerans in *Standards of Review Employed by Appellate Courts* (1994); and American Bar Association, Judicial Administration Division, *Standards Relating to Appellate Courts* (1995), at pp. 24-25).

The role of the appellate court was aptly defined in *Underwood v. Ocean City Realty Ltd.* (1987), 12 B.C.L.R. (2d) 199 (C.A.), at p. 204, where it was stated:

The appellate court must not retry a case and must not substitute its views for the views of the trial judge according to what the appellate court thinks the evidence establishes on its view of the balance of probabilities.

Gary D. Young, *c.r.*, *Denis I. Quon* et *M. Kim Anderson*, pour l'appelant.

Michael Morris et *G. L. Gerrand*, *c.r.*, pour l'intimée.

Version française du jugement du juge en chef McLachlin et des juges L'Heureux-Dubé, Iacobucci, Major et Arbour rendu par

LES JUGES IACOBUCCI ET MAJOR —

I. Introduction

Il va sans dire qu'une cour d'appel ne devrait modifier les conclusions d'un juge de première instance qu'en cas d'erreur manifeste et dominante. On reformule parfois cette proposition en disant qu'une cour d'appel ne peut réviser la décision du juge de première instance dans les cas où il existait des éléments de preuve qui pouvaient étayer cette décision. 1

Il existe une abondante jurisprudence étayant cette proposition, particulièrement des décisions émanant de cours d'appel, tant au Canada qu'à l'étranger (voir *Gottardo Properties (Dome) Inc. c. Toronto (City)* (1998), 162 D.L.R. (4th) 574 (C.A. Ont.); *Schwartz c. Canada*, [1996] 1 R.C.S. 254; *Toneguzzo-Norvell (Tutrice à l'instance de) c. Burnaby Hospital*, [1994] 1 R.C.S. 114; *Van de Perre c. Edwards*, [2001] 2 R.C.S. 1014, 2001 CSC 60). En outre, des auteurs, tant à l'échelle nationale qu'internationale, y souscrivent (voir C. A. Wright, « The Doubtful Omniscience of Appellate Courts » (1957), 41 *Minn. L. Rev.* 751, p. 780; l'honorable R. P. Kerans, *Standards of Review Employed by Appellate Courts* (1994); et American Bar Association, Judicial Administration Division, *Standards Relating to Appellate Courts* (1995), p. 24-25). 2

Le rôle des tribunaux d'appel a été défini de manière judicieuse dans l'arrêt *Underwood c. Ocean City Realty Ltd.* (1987), 12 B.C.L.R. (2d) 199 (C.A.), p. 204, où la cour a dit ceci : 3

[TRADUCTION] La cour d'appel ne doit pas juger l'affaire de nouveau, ni substituer son opinion à celle du juge de première instance en fonction de ce qu'elle pense que la preuve démontre, selon son opinion de la prépondérance des probabilités.

4 While the theory has acceptance, consistency in its application is missing. The foundation of the principle is as sound today as 100 years ago. It is premised on the notion that finality is an important aim of litigation. There is no suggestion that appellate court judges are somehow smarter and thus capable of reaching a better result. Their role is not to write better judgments but to review the reasons in light of the arguments of the parties and the relevant evidence, and then to uphold the decision unless a palpable error leading to a wrong result has been made by the trial judge.

Quoique cette théorie soit généralement acceptée, elle n'est pas appliquée de manière systématique. Le fondement de cette théorie est aussi valide aujourd'hui qu'il l'était il y a 100 ans. Cette théorie repose sur l'idée que le caractère définitif des décisions est un aspect important du processus judiciaire. Personne ne prétend que les juges des cours d'appel seraient, d'une manière ou d'une autre, plus intelligents que les autres et donc capables d'arriver à un meilleur résultat. Leur rôle n'est pas de rédiger de meilleurs jugements, mais de contrôler les motifs à la lumière des arguments des parties et de la preuve pertinente, puis de confirmer la décision à moins que le juge de première instance n'ait commis une erreur manifeste ayant conduit à un résultat erroné.

5 What is palpable error? The *New Oxford Dictionary of English* (1998) defines "palpable" as "clear to the mind or plain to see" (p. 1337). The *Cambridge International Dictionary of English* (1996) describes it as "so obvious that it can easily be seen or known" (p. 1020). The *Random House Dictionary of the English Language* (2nd ed. 1987) defines it as "readily or plainly seen" (p. 1399).

Qu'est-ce qu'une erreur manifeste? Le *Trésor de la langue française* (1985) définit ainsi le mot « manifeste » : « . . . Qui est tout à fait évident, qui ne peut être contesté dans sa nature ou son existence. [. . .] *erreur manifeste* » (p. 317). *Le Grand Robert de la langue française* (2e éd. 2001) définit ce mot ainsi : « Dont l'existence ou la nature est évidente. [. . .] Qui est clairement, évidemment tel. [. . .] *Erreur, injustice manifeste* » (p. 1139). Enfin, le *Grand Larousse de la langue française* (1975) donne la définition suivante de « manifeste » : « . . . Se dit d'une chose que l'on ne peut contester, qui est tout à fait évidente : *Une erreur manifeste* » (p. 3213).

6 The common element in each of these definitions is that palpable is plainly seen. Applying that to this appeal, in order for the Saskatchewan Court of Appeal to reverse the trial judge the "palpable and overriding" error of fact found by Cameron J.A. must be plainly seen. As we will discuss, we do not think that test has been met.

L'élément commun de ces définitions est qu'une chose « manifeste » est une chose qui est « évidente ». Si l'on applique ce critère au présent pourvoi, il faut que l'« erreur manifeste et dominante » décelée par le juge Cameron soit évidente pour que la Cour d'appel de la Saskatchewan puisse infirmer la décision de la juge de première instance. Comme nous le verrons plus loin, nous ne croyons pas qu'on a satisfait à ce critère en l'espèce.

II. The Role of the Appellate Court in the Case at Bar

II. Le rôle de la Cour d'appel en l'espèce

7 Given that an appeal is not a retrial of a case, consideration must be given to the applicable standard of review of an appellate court on the various issues which arise on this appeal. We therefore find it helpful to discuss briefly the standards of review relevant

Étant donné que l'appel ne constitue pas un nouveau procès, il faut se demander quelle est la norme de contrôle applicable en appel à l'égard des diverses questions que soulève le présent pourvoi. Nous estimons donc utile d'examiner brièvement

to the following types of questions: (1) questions of law; (2) questions of fact; (3) inferences of fact; and (4) questions of mixed fact and law.

A. *Standard of Review for Questions of Law*

On a pure question of law, the basic rule with respect to the review of a trial judge's findings is that an appellate court is free to replace the opinion of the trial judge with its own. Thus the standard of review on a question of law is that of correctness: Kerans, *supra*, at p. 90.

There are at least two underlying reasons for employing a correctness standard to matters of law. First, the principle of universality requires appellate courts to ensure that the same legal rules are applied in similar situations. The importance of this principle was recognized by this Court in *Woods Manufacturing Co. v. The King*, [1951] S.C.R. 504, at p. 515:

> It is fundamental to the due administration of justice that the authority of decisions be scrupulously respected by all courts upon which they are binding. Without this uniform and consistent adherence the administration of justice becomes disordered, the law becomes uncertain, and the confidence of the public in it undermined. Nothing is more important than that the law as pronounced . . . should be accepted and applied as our tradition requires; and even at the risk of that fallibility to which all judges are liable, we must maintain the complete integrity of relationship between the courts.

A second and related reason for applying a correctness standard to matters of law is the recognized law-making role of appellate courts which is pointed out by Kerans, *supra*, at p. 5:

> The call for universality, and the law-settling role it imposes, makes a considerable demand on a reviewing court. It expects from that authority a measure of expertise about the art of just and practical rule-making, an expertise that is not so critical for the first court. Reviewing courts, in cases where the law requires settlement, make law for future cases as well as the case under review.

les normes de contrôle se rapportant à chacune des catégories de questions suivantes : (1) les questions de droit; (2) les questions de fait; (3) les inférences de fait; (4) les questions mixtes de fait et de droit.

A. *La norme de contrôle applicable aux questions de droit*

Dans le cas des pures questions de droit, la règle fondamentale applicable en matière de contrôle des conclusions du juge de première instance est que les cours d'appel ont toute latitude pour substituer leur opinion à celle des juges de première instance. La norme de contrôle applicable à une question de droit est donc celle de la décision correcte : Kerans, *op. cit.*, p. 90.

Au moins deux raisons justifient l'application de la norme de la décision correcte aux questions de droit. Premièrement, le principe de l'universalité impose aux cours d'appel le devoir de veiller à ce que les mêmes règles de droit soient appliquées dans des situations similaires. Notre Cour a reconnu l'importance de ce principe dans *Woods Manufacturing Co. c. The King*, [1951] R.C.S. 504, p. 515 :

> [TRADUCTION] Il est fondamental, pour assurer la bonne administration de la justice, que l'autorité des décisions soit scrupuleusement respectée par tous les tribunaux qui sont liées par elles. Sans cette adhésion générale et constante, l'administration de la justice sera désordonnée, le droit deviendra incertain et la confiance dans celui-ci sera ébranlée. Il importe plus que tout que le droit, tel qu'il a été énoncé, [. . .] soit accepté et appliqué comme l'exige notre tradition; et même au risque de nous tromper, tous les juges étant faillibles, nous devons préserver totalement l'intégrité des rapports entre les tribunaux.

Une deuxième raison, connexe, d'appliquer la norme de la décision correcte aux questions de droit tient au rôle qu'on reconnaît aux cours d'appel en matière de création du droit et qu'a souligné Kerans, *op. cit.*, p. 5 :

> [TRADUCTION] Le principe de l'universalité — et le rôle de création du droit qu'il emporte — exige beaucoup du tribunal de révision. Il exige de ce tribunal qu'il fasse preuve d'un certain degré d'expertise dans l'art d'élaborer une règle de droit juste et pratique, expertise qui ne revêt pas une importance aussi cruciale pour le premier tribunal. Dans les affaires où le droit n'est pas fixé, le tribunal de révision élabore des règles de droit applicables tout autant à d'éventuelles affaires qu'à celle dont il est saisi.

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Thus, while the primary role of trial courts is to resolve individual disputes based on the facts before them and settled law, the primary role of appellate courts is to delineate and refine legal rules and ensure their universal application. In order to fulfill the above functions, appellate courts require a broad scope of review with respect to matters of law.

B. *Standard of Review for Findings of Fact*

10 The standard of review for findings of fact is that such findings are not to be reversed unless it can be established that the trial judge made a "palpable and overriding error": *Stein v. The Ship "Kathy K"*, [1976] 2 S.C.R. 802, at p. 808; *Ingles v. Tutkaluk Construction Ltd.*, [2000] 1 S.C.R. 298, 2000 SCC 12, at para. 42; *Ryan v. Victoria (City)*, [1999] 1 S.C.R. 201, at para. 57. While this standard is often cited, the principles underlying this high degree of deference rarely receive mention. We find it useful, for the purposes of this appeal, to review briefly the various policy reasons for employing a high level of appellate deference to findings of fact.

11 A fundamental reason for general deference to the trial judge is the presumption of fitness — a presumption that trial judges are just as competent as appellate judges to ensure that disputes are resolved justly. Kerans, *supra*, at pp. 10-11, states that:

> If we have confidence in these systems for the resolution of disputes, we should assume that those decisions are just. The appeal process is part of the decisional process, then, only because we recognize that, despite all effort, errors occur. An appeal should be the exception rather than the rule, as indeed it is in Canada.

12 With respect to findings of fact in particular, in *Gottardo Properties*, *supra*, Laskin J.A. summarized the purposes underlying a deferential stance as follows (at para. 48):

Ainsi, alors que le rôle premier des tribunaux de première instance consiste à résoudre des litiges sur la base des faits dont ils disposent et du droit établi, celui des cours d'appel est de préciser et de raffiner les règles de droit et de veiller à leur application universelle. Pour s'acquitter de ces rôles, les cours d'appel ont besoin d'un large pouvoir de contrôle à l'égard des questions de droit.

B. *La norme de contrôle applicable aux questions de fait*

Suivant la norme de contrôle applicable aux conclusions de fait, ces conclusions ne peuvent être infirmées que s'il est établi que le juge de première instance a commis une « erreur manifeste et dominante » : *Stein c. Le navire « Kathy K »*, [1976] 2 R.C.S. 802, p. 808; *Ingles c. Tutkaluk Construction Ltd.*, [2000] 1 R.C.S. 298, 2000 CSC 12, par. 42; *Ryan c. Victoria (Ville)*, [1999] 1 R.C.S. 201, par. 57. On cite souvent cette norme, mais rarement les principes justifiant ce degré élevé de retenue. Pour les besoins du présent pourvoi, nous estimons qu'il est utile d'examiner brièvement les diverses considérations de principe qui incitent les cours d'appel à faire preuve d'un degré élevé de retenue à l'égard des conclusions de fait.

L'une des raisons fondamentales de cette retenue générale à l'égard des conclusions des juges de première instance tient à la présomption d'aptitude à juger — présomption selon laquelle les juges de première instance sont tout aussi aptes que les juges d'appel à apporter des solutions justes aux litiges. Kerans, *op. cit.*, dit ceci aux p. 10-11 :

> [TRADUCTION] Si nous nous fions à ces systèmes pour régler les différends, il nous faut présumer que les décisions qu'ils produisent sont justes. La procédure d'appel ne fait en conséquence partie du processus décisionnel que parce que nous reconnaissons que, malgré tous les efforts déployés, des erreurs se produisent. L'appel devrait être l'exception plutôt que la règle, ce qui est d'ailleurs le cas au Canada.

Pour ce qui est des conclusions de fait en particulier, dans *Gottardo Properties*, précité, le juge Laskin de la Cour d'appel de l'Ontario a résumé ainsi les objectifs qui sous-tendent le principe de la retenue judiciaire (au par. 48) :

Deference is desirable for several reasons: to limit the number and length of appeals, to promote the autonomy and integrity of the trial or motion court proceedings on which substantial resources have been expended, to preserve the confidence of litigants in those proceedings, to recognize the competence of the trial judge or motion judge and to reduce needless duplication of judicial effort with no corresponding improvement in the quality of justice.

Similar concerns were expressed by La Forest J. in *Schwartz*, *supra*, at para. 32:

It has long been settled that appellate courts must treat a trial judge's findings of fact with great deference. The rule is principally based on the assumption that the trier of fact is in a privileged position to assess the credibility of witnesses' testimony at trial. . . . Others have also pointed out additional judicial policy concerns to justify the rule. Unlimited intervention by appellate courts would greatly increase the number and the length of appeals generally. Substantial resources are allocated to trial courts to go through the process of assessing facts. The autonomy and integrity of the trial process must be preserved by exercising deference towards the trial courts' findings of fact; see R. D. Gibbens, "Appellate Review of Findings of Fact" (1992), 13 *Adv. Q.* 445, at pp. 445-48; *Fletcher v. Manitoba Public Insurance Co.*, [1990] 3 S.C.R. 191, at p. 204.

See also in the context of patent litigation, *Consolboard Inc. v. MacMillan Bloedel (Saskatchewan) Ltd.*, [1981] 1 S.C.R. 504, at p. 537.

In *Anderson v. Bessemer City*, 470 U.S. 564 (1985), at pp. 574-75, the United States Supreme Court also listed numerous reasons for deferring to the factual findings of the trial judge:

The rationale for deference to the original finder of fact is not limited to the superiority of the trial judge's position to make determinations of credibility. The trial judge's major role is the determination of fact, and with experience in fulfilling that role comes expertise. Duplication of the trial judge's efforts in the court of appeals would very likely contribute only negligibly to the accuracy of fact determination at a huge cost in diversion of judicial resources. In addition, the parties to a case on appeal have already been forced to concentrate

[TRADUCTION] La retenue est souhaitable pour diverses raisons : pour limiter le nombre et la durée des appels, pour promouvoir l'autonomie et l'intégrité des procédures devant le tribunal de première instance ou la cour des requêtes auxquelles de nombreuses ressources ont été consacrées, pour maintenir la confiance des plaideurs, pour reconnaître la compétence du juge de première instance ou du juge des requêtes, et pour réduire la multiplication inutile des procédures qui n'entraînent aucune amélioration correspondante de la qualité de la justice.

Le juge La Forest a exprimé des préoccupations semblables dans l'arrêt *Schwartz*, précité, par. 32 :

Il est établi depuis longtemps que les cours d'appel doivent faire preuve d'une grande retenue à l'égard des conclusions de fait d'un juge de première instance. La règle se justifie principalement par la situation avantageuse dont bénéficie le juge des faits pour ce qui est d'évaluer la crédibilité des témoignages entendus au procès. [. . .] D'autres préoccupations liées à la politique judiciaire ont par ailleurs été invoquées pour justifier la règle. Une intervention illimitée des cours d'appel ferait augmenter considérablement le nombre et la durée des appels en général. D'importantes ressources sont mises à la disposition des tribunaux de première instance pour qu'ils puissent évaluer les faits. Il faut préserver l'autonomie et l'intégrité du procès en faisant preuve de retenue à l'égard des conclusions de fait des tribunaux de première instance; voir R. D. Gibbens, « Appellate Review of Findings of Fact » (1992), 13 *Adv. Q.* 445, aux pp. 445 à 448; *Fletcher c. Société d'assurance publique du Manitoba*, [1990] 3 R.C.S. 191, à la p. 204.

Voir aussi, dans le contexte d'une poursuite touchant un brevet, *Consolboard Inc. c. MacMillan Bloedel (Saskatchewan) Ltd.*, [1981] 1 R.C.S. 504, p. 537.

13 Dans *Anderson c. Bessemer City*, 470 U.S. 564 (1985), p. 574-575, la Cour suprême des États-Unis a aussi dressé une liste de raisons qui justifient de faire preuve de retenue à l'égard des conclusions de fait des juges de première instance :

[TRADUCTION] La raison d'être de la retenue à l'égard des conclusions de fait du juge de première instance ne se limite pas au fait que ce dernier est mieux placé pour statuer sur la crédibilité. Le rôle principal du juge de première instance est de constater les faits, et l'expérience qu'il acquiert en s'acquittant de ce rôle lui confère son expertise à cet égard. Si les cours d'appel refaisaient le travail du juge de première instance, il est fort possible que ces efforts n'amélioreraient que marginalement l'exactitude des conclusions de fait, malgré

their energies and resources on persuading the trial judge that their account of the facts is the correct one; requiring them to persuade three more judges at the appellate level is requiring too much. As the Court has stated in a different context, the trial on the merits should be "the 'main event' . . . rather than a 'tryout on the road.'" . . . For these reasons, review of factual findings under the clearly-erroneous standard — with its deference to the trier of fact — is the rule, not the exception.

14 Further comments regarding the advantages possessed by the trial judge have been made by R. D. Gibbens in "Appellate Review of Findings of Fact" (1991-92), 13 *Advocates' Q.* 445, at p. 446:

> The trial judge is said to have an expertise in assessing and weighing the facts developed at trial. Similarly, the trial judge has also been exposed to the entire case. The trial judge has sat through the entire case and his ultimate judgment reflects this total familiarity with the evidence. The insight gained by the trial judge who has lived with the case for several days, weeks or even months may be far deeper than that of the Court of Appeal whose view of the case is much more limited and narrow, often being shaped and distorted by the various orders or rulings being challenged.
>
> The corollary to this recognized advantage of trial courts and judges is that appellate courts are not in a favourable position to assess and determine factual matters. Appellate court judges are restricted to reviewing written transcripts of testimony. As well, appeals are unsuited to reviewing voluminous amounts of evidence. Finally, appeals are telescopic in nature, focussing narrowly on particular issues as opposed to viewing the case as a whole.

15 In our view, the numerous bases for deferring to the findings of fact of the trial judge which are discussed in the above authorities can be grouped into the following three basic principles.

(1) Limiting the Number, Length and Cost of Appeals

16 Given the scarcity of judicial resources, setting limits on the scope of judicial review is to be

les ressources judiciaires considérables qui devraient être réaffectées à cette fin. En outre, les parties à un appel ont déjà dû consacrer énergies et ressources à convaincre le juge de première instance de la justesse de leur version des faits; ce serait abuser que de leur demander de convaincre trois autres juges en appel. Comme l'a dit notre Cour dans un contexte différent, le procès sur le fond devrait être considéré comme « "l'épreuve principale" [. . .] plutôt que comme un "banc d'essai" ». [. . .] Pour ces motifs, le contrôle des décisions de fait selon la norme de la décision manifestement erronée — et la retenue envers le juge de première instance qu'elle suppose — est la règle, et non l'exception.

D'autres observations sur les avantages dont disposent le juge de première instance ont été formulées par R. D. Gibbens dans « Appellate Review of Findings of Fact » (1991-92), 13 *Advocates' Q.* 445, p. 446 :

> [TRADUCTION] On dit que le juge de première instance possède de l'expertise dans l'évaluation et l'appréciation des faits présentés au procès. Il a également entendu l'affaire au complet. Il a assisté à toute la cause et son jugement final reflète cette connaissance intime de la preuve. Cette connaissance, acquise par le juge au fil des jours, des semaines voire des mois qu'a durés l'affaire, peut se révéler beaucoup plus profonde que celle de la cour d'appel, dont la perception est beaucoup plus limitée et étroite, et souvent déterminée et déformée par les diverses ordonnances et décisions qui sont contestées.

Cet avantage reconnu des tribunaux et des juges de première instance a pour corollaire que les cours d'appel ne sont pas dans une position favorable pour évaluer et apprécier les questions de fait. Les juges des cours d'appel n'examinent que la transcription des témoignages. De plus, les appels ne se prêtent pas à l'examen de dossiers volumineux. Enfin, les appels ont un caractère « focalisateur », en ce qu'ils s'attachent à des questions particulières plutôt qu'à l'ensemble de l'affaire.

À notre avis, ces diverses raisons justifiant la retenue à l'égard des conclusions de fait du juge de première instance peuvent être regroupées sous les trois principes de base suivants.

(1) Réduire le nombre, la durée et le coût des appels

Vu la rareté des ressources dont disposent les tribunaux, il faut encourager l'établissement

encouraged. Deferring to a trial judge's findings of fact not only serves this end, but does so on a principled basis. Substantial resources are allocated to trial courts for the purpose of assessing facts. To allow for wide-ranging review of the trial judge's factual findings results in needless duplication of judicial proceedings with little, if any improvement in the result. In addition, lengthy appeals prejudice litigants with fewer resources, and frustrate the goal of providing an efficient and effective remedy for the parties.

(2) Promoting the Autonomy and Integrity of Trial Proceedings

The presumption underlying the structure of our court system is that a trial judge is competent to decide the case before him or her, and that a just and fair outcome will result from the trial process. Frequent and unlimited appeals would undermine this presumption and weaken public confidence in the trial process. An appeal is the exception rather than the rule.

(3) Recognizing the Expertise of the Trial Judge and His or Her Advantageous Position

The trial judge is better situated to make factual findings owing to his or her extensive exposure to the evidence, the advantage of hearing testimony *viva voce*, and the judge's familiarity with the case as a whole. Because the primary role of the trial judge is to weigh and assess voluminous quantities of evidence, the expertise and insight of the trial judge in this area should be respected.

C. *Standard of Review for Inferences of Fact*

We find it necessary to address the appropriate standard of review for factual inferences because the reasons of our colleague suggest that a lower standard of review may be applied to the inferences of fact drawn by a trial judge. With respect, it is our

de limites à la portée du contrôle judiciaire. La retenue à l'égard des conclusions de fait du juge de première instance sert cet objectif d'une manière rationnelle. D'importantes ressources sont allouées aux tribunaux de première instance aux fins d'évaluation des faits. Permettre un large contrôle des conclusions factuelles des juges de première instance entraîne une inutile répétition de procédures judiciaires, tout en n'améliorant que peu ou pas le résultat. En outre, de longs appels causent préjudice aux plaideurs moins bien nantis et compromettent l'objectif qui consiste à mettre à leur disposition des recours efficients et efficaces.

(2) Favoriser l'autonomie du procès et son intégrité

17 L'organisation de notre système judiciaire repose sur la présomption que le juge de première instance est qualifié pour trancher l'affaire dont il est saisi et qu'une solution juste et équitable résultera du procès. Des appels fréquents et illimités affaibliraient cette présomption et saperait la confiance du public dans le processus judiciaire. L'appel est l'exception, non la règle.

(3) Reconnaître l'expertise du juge de première instance et sa position avantageuse

18 Le juge de première instance est celui qui est le mieux placé pour tirer des conclusions de fait, parce qu'il a l'occasion d'examiner la preuve en profondeur, d'entendre les témoignages de vive voix et de se familiariser avec l'affaire dans son ensemble. Étant donné que le rôle principal du juge de première instance est d'apprécier et de soupeser d'abondantes quantités d'éléments de preuve, son expertise dans ce domaine et sa connaissance intime du dossier doivent être respectées.

C. *La norme de contrôle applicable aux inférences de fait*

19 Nous estimons nécessaire de nous pencher sur la question de la norme de contrôle appropriée quant aux inférences de fait des juges de première instance, parce que les motifs de notre collègue suggèrent qu'une norme de contrôle moins exigeante peut

view, that to apply a lower standard of review to inferences of fact would be to depart from established jurisprudence of this Court, and would be contrary to the principles supporting a deferential stance to matters of fact.

20 Our colleague acknowledges that, in *Geffen v. Goodman Estate*, [1991] 2 S.C.R. 353, this Court determined that a trial judge's inferences of fact and findings of fact should be accorded a similar degree of deference. The relevant passage from *Geffen* is the following (*per* Wilson J., at pp. 388-89):

> It is by now well established that findings of fact made at trial based on the credibility of witnesses are not to be reversed on appeal unless it is established that the trial judge made some palpable and overriding error which affected his assessment of the facts . . . . Even where a finding of fact is not contingent upon credibility, this Court has maintained a non-interventionist approach to the review of trial court findings. . . .
>
> And even in those cases where a finding of fact is neither inextricably linked to the credibility of the testifying witness nor based on a misapprehension of the evidence, the rule remains that appellate review should be limited to those instances where a manifest error has been made. Hence, in *Schreiber Brothers Ltd. v. Currie Products Ltd.*, [1980] 2 S.C.R. 78, this Court refused to overturn a trial judge's finding that certain goods were defective, stating at pp. 84-85 that it is wrong for an appellate court to set aside a trial judgment where the only point at issue is the interpretation of the evidence as a whole (citing *Métivier v. Cadorette*, [1977] 1 S.C.R. 371).

This view has been reiterated by this Court on numerous occasions: see *Palsky v. Humphrey*, [1964] S.C.R. 580, at p. 583; *Schwartz*, *supra*, at para. 32; *Hodgkinson v. Simms*, [1994] 3 S.C.R. 377, at p. 426, *per* La Forest J.; *Toneguzzo-Norvell*, *supra*. The United States Supreme Court has taken a similar position: see *Anderson*, *supra*, at p. 577.

21 In discussing the standard of review of the trial judge's inferences of fact, our colleague states, at para. 103, that:

être appliquée à cet égard. En toute déférence, nous sommes d'avis que l'application d'une telle norme de contrôle romprait avec la jurisprudence établie de notre Cour en la matière et serait contraire aux principes justifiant le respect d'une attitude empreinte de retenue à l'égard des constatations de fait.

Notre collègue reconnaît que dans l'arrêt *Geffen c. Succession Goodman*, [1991] 2 R.C.S. 353, notre Cour a jugé qu'il fallait faire preuve du même degré de retenue à l'égard des inférences de fait du juge de première instance qu'à l'égard de ses constatations de fait. Voici le passage pertinent des motifs de madame le juge Wilson (aux p. 388-389) :

> C'est maintenant un principe bien établi que les constatations de fait d'un juge de première instance, fondées sur la crédibilité des témoins, ne doivent pas être infirmées en appel à moins qu'il ne soit prouvé que le juge de première instance a commis une erreur manifeste et dominante qui a faussé son appréciation des faits [. . .] Même si une constatation de fait ne dépend pas de la crédibilité, notre Cour a pour principe de ne pas intervenir pour réviser les constatations des tribunaux de première instance . . .
>
> Et même dans les cas où une constatation de fait n'est ni liée inextricablement à la crédibilité du témoin ni fondée sur une mauvaise compréhension de la preuve, la règle reste la même : l'examen en appel devrait se limiter aux cas où une erreur manifeste a été commise. C'est pourquoi, dans l'arrêt *Schreiber Brothers Ltd. c. Currie Products Ltd.*, [1980] 2 R.C.S. 78, notre Cour a refusé d'infirmer la conclusion du juge de première instance que certaines marchandises étaient défectueuses, disant, aux pp. 84 et 85, qu'une cour d'appel ne peut à bon droit infirmer une décision de première instance lorsque la seule question en litige porte sur l'interprétation de l'ensemble de la preuve (citant *Métivier c. Cadorette*, [1977] 1 R.C.S. 371).

Notre Cour a réitéré cette opinion à maintes reprises : voir *Palsky c. Humphrey*, [1964] R.C.S. 580, p. 583; *Schwartz*, précité, par. 32; *Hodgkinson c. Simms*, [1994] 3 R.C.S. 377, p. 426, le juge La Forest; *Toneguzzo-Norvell*, précité. La Cour suprême des États-Unis a adopté une position semblable : voir *Anderson*, précité, p. 577.

Dans son examen de la norme de contrôle applicable aux inférences de fait du juge de première instance, notre collègue dit ce qui suit, au par. 103 :

In reviewing the making of an inference, the appeal court will verify whether it can reasonably be supported by the findings of fact that the trial judge reached and whether the judge proceeded on proper legal principles. . . . While the standard of review is identical for both findings of fact and inferences of fact, it is nonetheless important to draw an analytical distinction between the two. If the reviewing court were to review only for errors of fact, then the decision of the trial judge would necessarily be upheld in every case where evidence existed to support his or her factual findings. In my view, this Court is entitled to conclude that inferences made by the trial judge were clearly wrong, just as it is entitled to reach this conclusion in respect to findings of fact. [Emphasis added.]

With respect, we find two problems with this passage. First, in our view, the standard of review is not to verify that the inference can be reasonably supported by the findings of fact of the trial judge, but whether the trial judge made a palpable and overriding error in coming to a factual conclusion based on accepted facts, which implies a stricter standard.

Second, with respect, we find that by drawing an analytical distinction between factual findings and factual inferences, the above passage may lead appellate courts to involve themselves in an unjustified reweighing of the evidence. Although we agree that it is open to an appellate court to find that an inference of fact made by the trial judge is clearly wrong, we would add the caution that where evidence exists to support this inference, an appellate court will be hard pressed to find a palpable and overriding error. As stated above, trial courts are in an advantageous position when it comes to assessing and weighing vast quantities of evidence. In making a factual inference, the trial judge must sift through the relevant facts, decide on their weight, and draw a factual conclusion. Thus, where evidence exists which supports this conclusion, interference with this conclusion entails interference with the weight assigned by the trial judge to the pieces of evidence.

La cour d'appel qui contrôle la validité d'une inférence se demande si celle-ci peut raisonnablement être étayée par les conclusions de fait tirées par le juge de première instance et si celui-ci a appliqué les principes juridiques appropriés. [. . .] Bien que la norme de contrôle soit la même et pour les conclusions de fait et pour les inférences de fait, il importe néanmoins de faire une distinction analytique entre les deux. Si le tribunal de révision ne faisait que vérifier s'il y a des erreurs de fait, la décision du juge de première instance serait alors nécessairement confirmée dans tous les cas où il existe des éléments de preuve étayant les conclusions de fait de ce dernier. Selon moi, notre Cour a le droit de conclure que les inférences du juge de première instance étaient manifestement erronées, tout comme elle peut le faire à l'égard des conclusions de fait. [Nous soulignons.]

En toute déférence, nous estimons que ce passage comporte deux erreurs. Premièrement, selon nous, la norme de contrôle ne consiste pas à vérifier si l'inférence peut être raisonnablement étayée par les conclusions de fait du juge de première instance, mais plutôt si ce dernier a commis une erreur manifeste et dominante en tirant une conclusion factuelle sur la base de faits admis, ce qui suppose l'application d'une norme plus stricte.

22

Deuxièmement, nous croyons en toute déférence qu'en faisant une distinction analytique entre les conclusions factuelles et les inférences factuelles, le passage précité pourrait amener les cours d'appel à soupeser la preuve à nouveau et sans raison. Bien que nous partagions l'opinion selon laquelle il est loisible à une cour d'appel de conclure qu'une inférence de fait tirée par le juge de première instance est manifestement erronée, nous tenons toutefois à faire la mise en garde suivante : lorsque des éléments de preuve étayent cette inférence, il sera difficile à une cour d'appel de conclure à l'existence d'une erreur manifeste et dominante. Comme nous l'avons dit précédemment, les tribunaux de première instance sont dans une position avantageuse pour apprécier et soupeser de vastes quantités d'éléments de preuve. Pour tirer une inférence factuelle, le juge de première instance doit passer les faits pertinents au crible, en apprécier la valeur probante et tirer une conclusion factuelle. En conséquence, lorsque cette conclusion est étayée par des éléments de preuve, modifier cette conclusion équivaut à modifier le poids accordé à ces éléments par le juge de première instance.

23 We reiterate that it is not the role of appellate courts to second-guess the weight to be assigned to the various items of evidence. If there is no palpable and overriding error with respect to the underlying facts that the trial judge relies on to draw the inference, then it is only where the inference-drawing process itself is palpably in error that an appellate court can interfere with the factual conclusion. The appellate court is not free to interfere with a factual conclusion that it disagrees with where such disagreement stems from a difference of opinion over the weight to be assigned to the underlying facts. As we discuss below, it is our respectful view that our colleague's finding that the trial judge erred by imputing knowledge of the hazard to the municipality in this case is an example of this type of impermissible interference with the factual inference drawn by the trial judge.

24 In addition, in distinguishing inferences of fact from findings of fact, our colleague states, at para. 102, that deference to findings of fact is "principally grounded in the recognition that only the trial judge enjoys the opportunity to observe witnesses and to hear testimony first-hand", a rationale which does not bear on factual inferences. With respect, we disagree with this view. As we state above, there are numerous reasons for showing deference to the factual findings of a trial judge, many of which are equally applicable to all factual conclusions of the trial judge. This was pointed out in *Schwartz*, *supra*. After listing numerous policy concerns justifying a deferential approach to findings of fact, at para. 32 La Forest J. goes on to state:

> This explains why the rule [that appellate courts must treat a trial judge's findings of fact with great deference] applies not only when the credibility of witnesses is at issue, although in such a case it may be more strictly applied, but also to all conclusions of fact made by the trial judge. [Emphasis added.]

Nous rappelons qu'il n'appartient pas aux cours d'appel de remettre en question le poids attribué aux différents éléments de preuve. Si aucune erreur manifeste et dominante n'est décelée en ce qui concerne les faits sur lesquels repose l'inférence du juge de première instance, ce n'est que lorsque le processus inférentiel lui-même est manifestement erroné que la cour d'appel peut modifier la conclusion factuelle. La cour d'appel n'est pas habilitée à modifier une conclusion factuelle avec laquelle elle n'est pas d'accord, lorsque ce désaccord résulte d'une divergence d'opinion sur le poids à attribuer aux faits à la base de la conclusion. Comme nous le verrons plus loin, nous estimons en toute déférence que constitue un exemple de ce genre d'intervention inadmissible à l'égard d'une inférence de fait la conclusion de notre collègue selon laquelle la juge de première instance a commis une erreur en prêtant à la municipalité la connaissance du danger dans la présente affaire.

De plus, en établissant une distinction entre les inférences de fait et les conclusions de fait, notre collègue dit, au par. 102, que la retenue à l'égard des secondes « repose principalement sur le fait que, puisqu'il [le juge de première instance] est le seul à avoir l'occasion d'observer les témoins et d'entendre les témoignages de vive voix », justification non pertinente dans le cas des inférences de fait. En toute déférence, nous ne partageons pas cette opinion. Comme nous l'avons dit plus tôt, il existe de nombreuses raisons de faire preuve de retenue à l'égard des constatations de fait du juge de première instance, dont plusieurs valent autant pour toutes ses conclusions factuelles. Cette observation a été faite dans l'arrêt *Schwartz*, précité. Après avoir énuméré les nombreuses considérations de politique judiciaire invoquées pour justifier la règle de la retenue à l'égard des constatations de fait, le juge La Forest, au par. 32, ajoute :

> Cela explique pourquoi la règle [selon laquelle les cours d'appel doivent faire preuve d'une grande retenue à l'égard des conclusions de fait des juges de première instance] s'applique non seulement lorsque la crédibilité des témoins est en cause, quoiqu'elle puisse alors s'appliquer plus strictement, mais également à toutes les conclusions de fait tirées par le juge de première instance. [Nous soulignons.]

Recent support for deferring to all factual conclusions of the trial judge is found in *Toneguzzo-Norvell*, *supra.* McLachlin J. (as she then was) for a unanimous Court stated, at pp. 121-22:

> A Court of Appeal is clearly not entitled to interfere merely because it takes a different view of the evidence. The finding of facts and the drawing of evidentiary conclusions from facts is the province of the trial judge, not the Court of Appeal.
>
> . . .
>
> I agree that the principle of non-intervention of a Court of Appeal in a trial judge's findings of facts does not apply with the same force to inferences drawn from conflicting testimony of expert witnesses where the credibility of these witnesses is not in issue. This does not however change the fact that the weight to be assigned to the various pieces of evidence is under our trial system essentially the province of the trier of fact, in this case the trial judge. [Emphasis added.]

We take the above comments of McLachlin J. to mean that, although the same high standard of deference applies to the entire range of factual determinations made by the trial judge, where a factual finding is grounded in an assessment of credibility of a witness, the overwhelming advantage of the trial judge in this area must be acknowledged. This does not, however, imply that there is a lower standard of review where witness credibility is not in issue, or that there are not numerous policy reasons supporting deference to all factual conclusions of the trial judge. In our view, this is made clear by the underlined portion of the above passage. The essential point is that making a factual conclusion, of any kind, is inextricably linked with assigning weight to evidence, and thus attracts a deferential standard of review.

Although the trial judge will always be in a distinctly privileged position when it comes to

Notre Cour a récemment donné son appui à la règle de la retenue judiciaire à l'égard de l'ensemble des conclusions factuelles du juge de première instance dans l'arrêt *Toneguzzo-Norvell*, précité. Madame le juge McLachlin (maintenant Juge en chef), qui a rédigé le jugement unanime de notre Cour, a dit ceci, aux p. 121-122 :

> Une cour d'appel n'est manifestement pas autorisée à intervenir pour le simple motif qu'elle perçoit la preuve différemment. Il appartient au juge de première instance, et non à la cour d'appel, de tirer des conclusions de fait en matière de preuve.
>
> . . .
>
> Je reconnais que le principe de non-intervention d'une cour d'appel dans les conclusions de fait d'un juge de première instance ne s'applique pas avec la même vigueur aux conclusions tirées de témoignages d'expert contradictoires lorsque la crédibilité de ces derniers n'est pas en cause. Il n'en demeure pas moins que, selon notre système de procès, il appartient essentiellement au juge des faits, en l'espèce le juge de première instance, d'attribuer un poids aux différents éléments de preuve. [Nous soulignons.]

Nous considérons que ces propos du juge McLachlin signifient que, bien que le même degré élevé de retenue s'applique à l'ensemble des décisions factuelles du juge de première instance, lorsqu'une telle conclusion factuelle repose sur l'appréciation de la crédibilité d'un témoin, il faut reconnaître l'énorme avantage dont jouit le juge de première instance à cet égard. Cela ne veut toutefois pas dire qu'une norme de contrôle moins rigoureuse s'applique lorsque la question en jeu ne porte pas sur la crédibilité d'un témoin, ni qu'il n'existe pas de nombreuses considérations de principe justifiant de faire montre de retenue à l'égard de toutes les conclusions factuelles. À notre avis, cela ressort clairement du passage souligné dans l'extrait précité. Le point essentiel est qu'une conclusion factuelle — quelle que soit sa nature — exige nécessairement qu'on attribue un certain poids à un élément de preuve et, de ce fait, commande l'application d'une norme de contrôle empreinte de retenue.

Bien que le juge de première instance soit toujours dans une position privilégiée pour apprécier

assessing the credibility of witnesses, this is not the only area where the trial judge has an advantage over appellate judges. Advantages enjoyed by the trial judge with respect to the drawing of factual inferences include the trial judge's relative expertise with respect to the weighing and assessing of evidence, and the trial judge's inimitable familiarity with the often vast quantities of evidence. This extensive exposure to the entire factual nexus of a case will be of invaluable assistance when it comes to drawing factual conclusions. In addition, concerns with respect to cost, number and length of appeals apply equally to inferences of fact and findings of fact, and support a deferential approach towards both. As such, we respectfully disagree with our colleague's view that the principal rationale for showing deference to findings of fact is the opportunity to observe witnesses first-hand. It is our view that the trial judge enjoys numerous advantages over appellate judges which bear on all conclusions of fact, and, even in the absence of these advantages, there are other compelling policy reasons supporting a deferential approach to inferences of fact. We conclude, therefore, by emphasizing that there is one, and only one, standard of review applicable to all factual conclusions made by the trial judge — that of palpable and overriding error.

la crédibilité des témoins, ce n'est pas là le seul domaine où il bénéficie d'un avantage sur les juges des cours d'appel. Parmi les avantages dont jouit le juge de première instance sur le plan des inférences factuelles, mentionnons son expertise relative en matière d'appréciation et d'évaluation de la preuve, de même que la connaissance unique qu'il possède de la preuve souvent abondante produite par les parties. Cette familiarité avec toute la trame factuelle lui est d'une grande utilité lorsque vient le moment de tirer des conclusions de fait. En outre, les considérations relatives au coût, au nombre et à la durée des appels sont tout aussi pertinentes pour ce qui est des inférences de fait que pour ce qui est des conclusions de fait, et justifient l'application aux unes comme aux autres d'une norme empreinte de retenue. En conséquence, nous ne partageons pas l'opinion de notre collègue selon laquelle la raison principale justifiant de faire montre de retenue à l'égard des conclusions de fait est la possibilité qu'a le juge de première instance d'observer les témoins directement. Nous sommes d'avis que le juge de première instance jouit, par rapport aux juges d'appel, de nombreux avantages qui influent sur toutes les conclusions de fait et que, même si ces avantages n'existaient pas, d'autres considérations impérieuses justifient de faire montre de retenue à l'égard des inférences de fait. Par conséquent, nous concluons en soulignant qu'il n'y a qu'une seule et unique norme de contrôle applicable à toutes les conclusions factuelles tirées par le juge de première instance, soit celle de l'erreur manifeste et dominante.

D. *Standard of Review for Questions of Mixed Fact and Law*

26 At the outset, it is important to distinguish questions of mixed fact and law from factual findings (whether direct findings or inferences). Questions of mixed fact and law involve applying a legal standard to a set of facts: *Canada (Director of Investigation and Research) v. Southam Inc.*, [1997] 1 S.C.R. 748, at para. 35. On the other hand, factual findings or inferences require making a conclusion of fact based on a set of facts. Both mixed fact and law and fact findings often involve drawing inferences; the difference lies in whether the inference drawn is legal

D. *La norme de contrôle applicable aux questions mixtes de fait et de droit*

D'entrée de jeu, il importe de distinguer les questions mixtes de fait et de droit des conclusions factuelles (qu'il s'agisse de conclusions directes ou d'inférences). Les questions mixtes de fait et de droit supposent l'application d'une norme juridique à un ensemble de faits : *Canada (Directeur des enquêtes et des recherches) c. Southam Inc.*, [1997] 1 R.C.S. 748, par. 35. Par contre, les conclusions ou les inférences de fait exigent que soit tirée une conclusion factuelle d'un ensemble de faits. Tant les questions mixtes de fait et de droit que les questions

or factual. Because of this similarity, the two types of questions are sometimes confounded. This confusion was pointed out by A. L. Goodhart in "Appeals on Questions of Fact" (1955), 71 *L.Q.R.* 402, at p. 405:

> The distinction between [the perception of facts and the evaluation of facts] tends to be obfuscated because we use such a phrase as "the judge found as a fact that the defendant had been negligent," when what we mean to say is that "the judge found as a fact that the defendant had done acts A and B, and as a matter of opinion he reached the conclusion that it was not reasonable for the defendant to have acted in that way."

In the case at bar, there are examples of both types of questions. The issue of whether the municipality ought to have known of the hazard in the road involves weighing the underlying facts and making factual findings as to the knowledge of the municipality. It also involves applying a legal standard, which in this case is provided by s. 192(3) of the *Rural Municipality Act, 1989*, S.S. 1989-90, c. R-26.1, to these factual findings. Similarly, the finding of negligence involves weighing the underlying facts, making factual conclusions therefrom, and drawing an inference as to whether or not the municipality failed to exercise the legal standard of reasonable care and therefore was negligent.

Once it has been determined that a matter being reviewed involves the application of a legal standard to a set of facts, and is thus a question of mixed fact and law, then the appropriate standard of review must be determined and applied. Given the different standards of review applicable to questions of law and questions of fact, it is often difficult to determine what the applicable standard of review is. In *Southam*, *supra*, at para. 39, this Court illustrated how an error on a question of mixed fact and law can amount to a pure error of law subject to the correctness standard:

> . . . if a decision-maker says that the correct test requires him or her to consider A, B, C, and D, but in fact the

de fait exigent souvent du tribunal qu'il tire des inférences; la différence réside dans le caractère — juridique ou factuel — de ces inférences. En raison de cette similitude, on confond parfois les deux catégories de questions. Cette confusion a été soulignée par A. L. Goodhart dans « Appeals on Questions of Fact » (1955), 71 *L.Q.R.* 402, p. 405 :

> [TRADUCTION] La distinction entre [la perception des faits et l'appréciation de ceux-ci] a tendance à être embrouillée parce que nous utilisons la formule « le juge a conclu au fait que le défendeur avait été négligent », alors que ce que nous voulons dire, c'est que « le juge a constaté le fait que le défendeur a commis les actes A et B et, suivant son opinion, il a conclu qu'il n'était pas raisonnable pour ce dernier d'avoir agi ainsi ».

L'affaire qui nous occupe présente des exemples des deux catégories de questions. Pour répondre à la question de savoir si la municipalité aurait dû connaître le danger présenté par le chemin, il faut apprécier les faits à l'origine de l'affaire et tirer des conclusions factuelles relativement à la connaissance de la municipalité. Il faut appliquer à ces conclusions factuelles une norme juridique qui, en l'occurrence, est énoncée au par. 192(3) de la *Rural Municipality Act, 1989*, S.S. 1989-90, ch. R-26.1. De même, pour pouvoir conclure à la négligence, il faut apprécier les faits essentiels, en tirer des conclusions factuelles puis en dégager une inférence, c'est-à-dire se demander si la municipalité a oui ou non omis de respecter la norme de diligence raisonnable et si elle a, par conséquent, été négligente ou non.

27

Une fois établi que la question examinée exige l'application d'une norme juridique à un ensemble de faits et qu'il s'agit donc d'une question mixte de fait et de droit, il faut alors déterminer quelle est la norme de contrôle appropriée et l'appliquer. Vu les diverses normes de contrôle qui s'appliquent aux questions de droit et aux questions de fait, il est souvent difficile de déterminer celle qui s'applique. Dans l'arrêt *Southam*, précité, par. 39, notre Cour a expliqué comment une erreur touchant une question mixte de fait et de droit peut constituer une pure erreur de droit, assujettie à la norme de la décision correcte :

> . . . si un décideur dit que, en vertu du critère applicable, il lui faut tenir compte de A, B, C et D, mais que, dans les

decision-maker considers only A, B, and C, then the outcome is as if he or she had applied a law that required consideration of only A, B, and C. If the correct test requires him or her to consider D as well, then the decision-maker has in effect applied the wrong law, and so has made an error of law.

Therefore, what appears to be a question of mixed fact and law, upon further reflection, can actually be an error of pure law.

28 However, where the error does not amount to an error of law, a higher standard is mandated. Where the trier of fact has considered all the evidence that the law requires him or her to consider and still comes to the wrong conclusion, then this amounts to an error of mixed law and fact and is subject to a more stringent standard of review: *Southam*, *supra*, at paras. 41 and 45. While easy to state, this distinction can be difficult in practice because matters of mixed law and fact fall along a spectrum of particularity. This difficulty was pointed out in *Southam*, at para. 37:

> . . . the matrices of facts at issue in some cases are so particular, indeed so unique, that decisions about whether they satisfy legal tests do not have any great precedential value. If a court were to decide that driving at a certain speed on a certain road under certain conditions was negligent, its decision would not have any great value as a precedent. In short, as the level of generality of the challenged proposition approaches utter particularity, the matter approaches pure application, and hence draws nigh to being an unqualified question of mixed law and fact. See R. P. Kerans, *Standards of Review Employed by Appellate Courts* (1994), at pp. 103-108. Of course, it is not easy to say precisely where the line should be drawn; though in most cases it should be sufficiently clear whether the dispute is over a general proposition that might qualify as a principle of law or over a very particular set of circumstances that is not apt to be of much interest to judges and lawyers in the future.

29 When the question of mixed fact and law at issue is a finding of negligence, this Court has held that

faits, il ne prend en considération que A, B, et C, alors le résultat est le même que s'il avait appliqué une règle de droit lui dictant de ne tenir compte que de A, B et C. Si le bon critère lui commandait de tenir compte aussi de D, il a en fait appliqué la mauvaise règle de droit et commis, de ce fait, une erreur de droit.

Par conséquent, ce qui peut paraître une question mixte de fait et de droit peut, après plus ample examen, se révéler en réalité une pure erreur de droit.

Cependant, lorsque l'erreur ne constitue pas une erreur de droit, une norme de contrôle plus exigeante s'impose. Dans les cas où le juge des faits examine tous les éléments de preuve que le droit lui commande de prendre en considération mais en tire néanmoins une conclusion erronée, il commet alors une erreur mixte de fait et de droit, qui est assujettie à une norme de contrôle plus rigoureuse : *Southam*, précité, par. 41 et 45. Bien que facile à énoncer, cette distinction peut s'avérer difficile à établir en pratique parce que les questions mixtes de fait et de droit s'étalent le long d'un spectre comportant des degrés variables de particularité. Cette difficulté a été soulignée dans l'arrêt *Southam*, par. 37 :

> . . . il arrive que les faits dans certaines affaires soient si particuliers, de fait qu'ils soient si uniques, que les décisions concernant la question de savoir s'ils satisfont aux critères juridiques n'ont pas une grande valeur comme précédents. Si une cour décidait que le fait d'avoir conduit à une certaine vitesse, sur une route donnée et dans des conditions particulières constituait de la négligence, sa décision aurait peu de valeur comme précédent. Bref, plus le niveau de généralité de la proposition contestée se rapproche de la particularité absolue, plus l'affaire prend le caractère d'une question d'application pure, et s'approche donc d'une question de droit et de fait parfaite. Voir R. P. Kerans, *Standards of Review Employed by Appellate Courts* (1994), aux pp. 103 à 108. Il va de soi qu'il n'est pas facile de dire avec précision où doit être tracée la ligne de démarcation; quoique, dans la plupart des cas, la situation soit suffisamment claire pour permettre de déterminer si le litige porte sur une proposition générale qui peut être qualifiée de principe de droit ou sur un ensemble très particulier de circonstances qui n'est pas susceptible de présenter beaucoup d'intérêt pour les juges et les avocats dans l'avenir.

Lorsque la question mixte de fait et de droit en litige est une conclusion de négligence, notre

a finding of negligence by the trial judge should be deferred to by appellate courts. In *Jaegli Enterprises Ltd. v. Taylor*, [1981] 2 S.C.R. 2, at p. 4, Dickson J. (as he then was) set aside the holding of the British Columbia Court of Appeal that the trial judge had erred in his finding of negligence on the basis that "it is wrong for an appellate court to set aside a trial judgment where there is not palpable and overriding error, and the only point at issue is the interpretation of the evidence as a whole" (see also *Schreiber Brothers Ltd. v. Currie Products Ltd.*, [1980] 2 S.C.R. 78, at p. 84).

Cour a jugé que les cours d'appel devaient faire preuve de retenue à l'égard de la conclusion du juge de première instance. Dans l'arrêt *Jaegli Enterprises Ltd. c. Taylor*, [1981] 2 R.C.S. 2, p. 4, le juge Dickson (plus tard Juge en chef) a infirmé la décision de la Cour d'appel de la Colombie-Britannique portant que le juge de première instance avait erronément conclu à la négligence, pour le motif qu'« une cour d'appel commet une erreur lorsqu'elle infirme un jugement de première instance s'il n'y a pas une erreur manifeste et dominante, et si l'interprétation de l'ensemble de la preuve est le seul point en litige » (voir aussi l'arrêt *Schreiber Brothers Ltd. c. Currie Products Ltd.*, [1980] 2 R.C.S. 78, p. 84).

This more stringent standard of review for findings of negligence is appropriate, given that findings of negligence at the trial level can also be made by juries. If the standard were instead correctness, this would result in the appellate court assessing even jury findings of negligence on a correctness standard. At present, absent misdirection on law by the trial judge, such review is not available. The general rule is that courts accord great deference to a jury's findings in civil negligence proceedings:

30

Il convient d'appliquer cette norme de contrôle plus exigeante aux conclusions de négligence, étant donné que de telles conclusions peuvent également être tirées par des jurys en première instance. Si la norme applicable était celle de la décision correcte, il s'ensuivrait que les cours d'appel appliqueraient cette norme pour contrôler même des conclusions de négligence tirées par jurys. Actuellement, il n'y a ouverture à un tel contrôle que si le juge du procès a donné des directives erronées au jury sur le droit applicable. Suivant la règle générale, les tribunaux font montre d'une grande retenue envers les conclusions des jurys dans les procès civils pour négligence :

> The principle has been laid down in many judgments of this Court to this effect, that the verdict of a jury will not be set aside as against the weight of evidence unless it is so plainly unreasonable and unjust as to satisfy the Court that no jury reviewing the evidence as a whole and acting judicially could have reached it.
>
> (*McCannell v. McLean*, [1937] S.C.R. 341, at p. 343)

> [TRADUCTION] Le principe pertinent a été énoncé dans bon nombre d'arrêts de notre Cour, à savoir qu'il n'y a pas lieu d'écarter le verdict d'un jury parce qu'il va à l'encontre du poids de la preuve, à moins que le verdict en question ne soit nettement déraisonnable et injuste au point de convaincre le tribunal qu'aucun jury examinant la preuve dans son ensemble et agissant de façon judiciaire n'aurait pu le prononcer.
>
> (*McCannell c. McLean*, [1937] R.C.S. 341, p. 343)

See also *Dube v. Labar*, [1986] 1 S.C.R. 649, at p. 662, and *C.N.R. v. Muller*, [1934] 1 D.L.R. 768 (S.C.C.). To adopt a correctness standard would change the law and undermine the traditional function of the jury. Therefore, requiring a standard of "palpable and overriding error" for findings of negligence made by either a trial judge or a jury rein-

Voir également *Dube c. Labar*, [1986] 1 R.C.S. 649, p. 662, et *C.N.R. c. Muller*, [1934] 1 D.L.R. 768 (C.S.C.). Adopter la norme de la décision correcte aurait pour effet de modifier le droit et de porter atteinte au rôle traditionnel du jury. Par conséquent, le fait d'exiger l'application de la norme de l'« erreur manifeste et dominante » aux

forces the proper relationship between the appellate and trial court levels and accords with the established standard of review applicable to a finding of negligence by a jury.

31 Where, however, the erroneous finding of negligence of the trial judge rests on an incorrect statement of the legal standard, this can amount to an error of law. This distinction was pointed out by Cory J. in *Galaske v. O'Donnell*, [1994] 1 S.C.R 670, at pp. 690-91:

> The definition of the standard of care is a mixed question of law and fact. It will usually be for the trial judge to determine, in light of the circumstances of the case, what would constitute reasonable conduct on the part of the legendary reasonable man placed in the same circumstances. In some situations a simple reminder may suffice while in others, for example when a very young child is the passenger, the driver may have to put the seat belt on the child himself. In this case, however, the driver took no steps whatsoever to ensure that the child passenger wore a seat belt. It follows that the trial judge's decision on the issue amounted to a finding that there was no duty at all resting upon the driver. This was an error of law.

Galaske, *supra*, is an illustration of the point made in *Southam*, *supra*, of the potential to extricate a purely legal question from what appears to be a question of mixed fact and law. However, in the absence of a legal error or a palpable and overriding error, a finding of negligence by a trial judge should not be interfered with.

32 We are supported in our conclusion by the analogy which can be drawn between inferences of fact and questions of mixed fact and law. As stated above, both involve drawing inferences from underlying facts. The difference lies in whether the inference drawn relates to a legal standard or not. Because both processes are intertwined with the weight assigned to the evidence, the numerous policy reasons which support a deferential stance to the trial judge's inferences of fact, also, to a certain extent, support showing

fins de contrôle d'une conclusion de négligence tirée par un juge ou un jury consolide les rapports qui doivent exister entre les juridictions d'appel et celles de première instance et respecte la norme de contrôle bien établie qui s'applique aux conclusions de négligence tirées par les jurys.

Toutefois, lorsque le juge du procès conclut erronément à la négligence par suite d'une formulation incorrecte de la norme juridique, cela peut constituer une erreur de droit. Cette distinction a été faite par le juge Cory dans l'arrêt *Galaske c. O'Donnell*, [1994] 1 R.C.S. 670, p. 690-691 :

> La définition de la norme de diligence est une question mixte de droit et de fait. Il incombera habituellement au juge du procès de déterminer, compte tenu des circonstances de l'espèce, ce qui constituerait une conduite raisonnable de la part de la personne raisonnable légendaire placée dans la même situation. Dans certains cas, un simple rappel suffira, tandis que dans d'autres, par exemple lorsqu'un très jeune enfant est passager, le conducteur peut avoir à attacher lui-même la ceinture de sécurité de l'enfant. Cependant, en l'espèce, le conducteur n'a pris aucune mesure pour veiller à ce que l'enfant porte sa ceinture de sécurité. Il s'ensuit que la décision du juge du procès sur la question équivalait à une conclusion qu'aucune obligation n'incombait au conducteur, ce qui constituait une erreur de droit.

L'arrêt *Galaske*, précité, illustre bien l'idée exposée dans l'arrêt *Southam*, précité, selon laquelle il est possible de dégager une pure question de droit de ce qui paraît être une question mixte de fait et de droit. Toutefois, en l'absence d'erreur de droit ou d'une erreur manifeste et dominante, la conclusion de négligence tirée par un juge de première instance ne doit pas être modifiée.

L'analogie qui peut être établie entre les inférences de fait et les questions mixtes de fait et de droit étaye notre conclusion. Comme nous l'avons dit précédemment, dans les deux cas des inférences doivent être tirées des faits à l'origine de l'affaire. La différence dépend de la question de savoir si l'inférence se rapporte à une norme juridique ou non. Parce que le résultat des deux processus est tributaire du poids accordé à la preuve, les diverses considérations de principe justifiant de faire montre de retenue à l'égard des inférences de

deference to the trial judge's inferences of mixed fact and law.

Where, however, an erroneous finding of the trial judge can be traced to an error in his or her characterization of the legal standard, then this encroaches on the law-making role of an appellate court, and less deference is required, consistent with a "correctness" standard of review. This nuance was recognized by this Court in *St-Jean v. Mercier*, [2002] 1 S.C.R. 491, 2002 SCC 15, at paras. 48-49:

> A question "about whether the facts satisfy the legal tests" is one of mixed law and fact. Stated differently, "whether the defendant satisfied the appropriate standard of care is a question of mixed law and fact" (*Southam*, at para. 35).
>
> Generally, such a question, once the facts have been established without overriding and palpable error, is to be reviewed on a standard of correctness since the standard of care is normative and is a question of law within the normal purview of both the trial and appellate courts. [Emphasis added.]

A good example of this subtle principle can be found in *Rhône (The) v. Peter A.B. Widener (The)*, [1993] 1 S.C.R. 497, at pp. 515-16. In that case the issue was the identification of certain individuals within a corporate structure as directing minds. This is a mixed question of law and fact. However, the erroneous finding of the courts below was easily traceable to an error of law which could be extricated from the mixed question of law and fact. The extricable question of law was the issue of the functions which are required in order to be properly identified as a "directing mind" within a corporate structure (pp. 515-16). In the opinion of Iacobucci J. for the majority of the Court (at p. 526):

> With respect, I think that the courts below overemphasized the significance of sub-delegation in this case. The key factor which distinguishes directing minds from normal employees is the capacity to exercise decision-making authority on matters of corporate policy, rather than merely to give effect to such policy on an

fait du juge de première instance justifient également, dans une certaine mesure, de faire de même à l'égard de ses inférences mixtes de fait et de droit.

33 Par contre, lorsqu'il peut être établi que la conclusion erronée du juge de première instance découle d'une erreur quant à la norme juridique à appliquer, ce facteur touche au rôle de création du droit de la cour d'appel, et une retenue moins élevée s'impose, conformément à la norme de la décision « correcte ». Notre Cour a apporté cette nuance dans l'arrêt *St-Jean c. Mercier*, [2002] 1 R.C.S. 491, 2002 CSC 15, par. 48-49 :

> La question qui consiste « à déterminer si les faits satisfont au critère juridique » est une question mixte de droit et de fait ou, en d'autres termes, « la question de savoir si le défendeur a respecté la norme de diligence appropriée est une question de droit et de fait » (*Southam*, par. 35).
>
> Une fois les faits établis sans erreur manifeste et dominante, cette question doit généralement être révisée suivant la norme de la décision correcte puisque la norme de diligence est normative et constitue une question de droit qui relève de la compétence habituelle des tribunaux de première instance et d'appel. [Nous soulignons.]

34 Un bon exemple de ce principe subtil est l'arrêt *Rhône (Le) c. Peter A.B. Widener (Le)*, [1993] 1 R.C.S. 497, p. 515-516. La question en litige dans cette affaire consistait à déterminer si certaines personnes faisaient partie des âmes dirigeantes d'une société. Il s'agit d'une question mixte de droit et de fait. Toutefois, la conclusion erronée des juridictions inférieures était facilement imputable à une erreur de droit qui pouvait être dégagée de la question mixte de droit et de fait. La question de droit ainsi isolable était celle des fonctions que devait remplir une personne pour qu'on puisse à bon droit la considérer comme une « âme dirigeante » de la société (p. 515-516). Le juge Iacobucci s'est exprimé ainsi au nom des juges de la majorité, à la p. 526 :

> En toute déférence, je crois que les juridictions inférieures ont trop insisté sur l'importance de la subdélégation en l'espèce. Le facteur clé qui permet de distinguer les âmes dirigeantes des employés ordinaires est la capacité d'exercer un pouvoir décisionnel sur les questions de politique générale de la personne morale, plutôt que

operational basis, whether at head office or across the sea.

35 Stated differently, the lower courts committed an error in law by finding that sub-delegation was a factor identifying a person who is part of the "directing mind" of a company, when the correct legal factor characterizing a "directing mind" is in fact "the capacity to exercise decision-making authority on matters of corporate policy". This mischaracterization of the proper legal test (the legal requirements to be a "directing mind") infected or tainted the lower courts' factual conclusion that Captain Kelch was part of the directing mind. As this erroneous finding can be traced to an error in law, less deference was required and the applicable standard was one of correctness.

36 To summarize, a finding of negligence by a trial judge involves applying a legal standard to a set of facts, and thus is a question of mixed fact and law. Matters of mixed fact and law lie along a spectrum. Where, for instance, an error with respect to a finding of negligence can be attributed to the application of an incorrect standard, a failure to consider a required element of a legal test, or similar error in principle, such an error can be characterized as an error of law, subject to a standard of correctness. Appellate courts must be cautious, however, in finding that a trial judge erred in law in his or her determination of negligence, as it is often difficult to extricate the legal questions from the factual. It is for this reason that these matters are referred to as questions of "mixed law and fact". Where the legal principle is not readily extricable, then the matter is one of "mixed law and fact" and is subject to a more stringent standard. The general rule, as stated in *Jaegli Enterprises*, *supra*, is that, where the issue on appeal involves the trial judge's interpretation of the evidence as a whole, it should not be overturned absent palpable and overriding error.

le simple fait de mettre en œuvre ces politiques dans un cadre opérationnel, que ce soit au siège social ou en mer.

En d'autres termes, les juridictions inférieures ont commis une erreur de droit en concluant que la subdélégation était un facteur permettant de qualifier une personne d'« âme dirigeante » d'une société, alors que le facteur juridique applicable à cet égard est en fait « la capacité d'exercer un pouvoir décisionnel sur les questions de politique générale de la personne morale ». Cette formulation erronée du critère juridique approprié (les conditions juridiques requises pour être une « âme dirigeante ») a entaché ou vicié la conclusion factuelle des juridictions inférieures selon laquelle le capitaine Kelch était une âme dirigeante de la société. Comme cette conclusion erronée était imputable à une erreur de droit, un degré moindre de retenue s'imposait et la norme applicable était celle de la décision correcte.

En résumé, la conclusion de négligence que tire le juge de première instance suppose l'application d'une norme juridique à un ensemble de faits et constitue donc une question mixte de fait et de droit. Les questions mixtes de fait et de droit s'étalent le long d'un spectre. Lorsque, par exemple, la conclusion de négligence est entachée d'une erreur imputable à l'application d'une norme incorrecte, à l'omission de tenir compte d'un élément essentiel d'un critère juridique ou à une autre erreur de principe semblable, une telle erreur peut être qualifiée d'erreur de droit et elle est contrôlée suivant la norme de la décision correcte. Les cours d'appel doivent cependant faire preuve de prudence avant de juger que le juge de première instance a commis une erreur de droit lorsqu'il a conclu à la négligence, puisqu'il est souvent difficile de départager les questions de droit et les questions de fait. Voilà pourquoi on appelle certaines questions des questions « mixtes de fait et de droit ». Si le principe juridique n'est pas facilement isolable, il s'agit alors d'une « question mixte de fait et de droit », assujettie à une norme de contrôle plus rigoureuse. Selon la règle générale énoncée dans l'arrêt *Jaegli Enterprises*, précité, si la question litigieuse en appel soulève l'interprétation de l'ensemble de la preuve par le juge de première instance, cette interprétation ne doit pas être infirmée en l'absence d'erreur manifeste et dominante.

In this regard, we respectfully disagree with our colleague when he states at para. 106 that "[o]nce the facts have been established, the determination of whether or not the standard of care was met by the defendant will in most cases be reviewable on a standard of correctness since the trial judge must appreciate the facts within the context of the appropriate standard of care. In many cases, viewing the facts through the legal lens of the standard of care gives rise to a policy-making or law-setting function that is the purview of both the trial and appellate courts". In our view, it is settled law that the determination of whether or not the standard of care was met by the defendant involves the application of a legal standard to a set of facts, a question of mixed fact and law. This question is subject to a standard of palpable and overriding error unless it is clear that the trial judge made some extricable error in principle with respect to the characterization of the standard or its application, in which case the error may amount to an error of law.

III. Application of the Foregoing Principles to this Case: Standard of Care of the Municipality

A. *The Appropriate Standard of Review*

We agree with our colleague that the correct statement of the municipality's standard of care is that found in *Partridge v. Rural Municipality of Langenburg*, [1929] 3 W.W.R. 555 (Sask. C.A.), *per* Martin J.A., at pp. 558-59:

> The extent of the statutory obligation placed upon municipal corporations to keep in repair the highways under their jurisdiction, has been variously stated in numerous reported cases. There is, however, a general rule which may be gathered from the decisions, and that is, that the road must be kept in such a reasonable state of repair that those requiring to use it may, exercising ordinary care, travel upon it with safety. What is a reasonable state of repair is a question of fact, depending upon all the surrounding circumstances; "repair" is a relative term, and hence the facts in one case afford no fixed rule

37 À cet égard, nous ne pouvons en toute déférence pas souscrire à l'opinion de notre collègue lorsqu'il affirme, au par. 106, qu'« [u]ne fois les faits établis, la décision touchant la question de savoir si le défendeur a respecté ou non la norme de diligence est, dans la plupart des cas, contrôlable selon la norme de la décision correcte, puisque le juge de première instance doit apprécier les faits au regard de la norme de diligence appropriée. Dans bien des cas, l'examen des faits à travers le prisme juridique de la norme de diligence implique l'établissement de politiques d'intérêt général ou la création de règles de droit, rôle qui relève autant des cours de première instance que des cours d'appel ». À notre avis, il est bien établi en droit que la question de savoir si le défendeur a respecté la norme de diligence suppose l'application d'une norme juridique à un ensemble de faits, ce qui en fait une question mixte de fait et de droit. Cette question est assujettie à la norme de l'erreur manifeste et dominante, à moins que le juge de première instance n'ait clairement commis une erreur de principe isolable en déterminant la norme applicable ou en appliquant cette norme, auquel cas l'erreur peut constituer une erreur de droit.

III. Application des principes qui précèdent à l'espèce : la norme de diligence applicable à la municipalité

A. *La norme de contrôle appropriée*

38 À l'instar de notre collègue, nous sommes d'avis que la norme de diligence applicable à la municipalité a été convenablement énoncée par le juge Martin dans l'arrêt *Partridge c. Rural Municipality of Langenburg*, [1929] 3 W.W.R. 555 (C.A. Sask.), p. 558-559 :

> [TRADUCTION] L'étendue de l'obligation légale d'entretien qui incombe aux corporations municipales à l'égard des routes qui se trouvent sur leur territoire a été énoncée de diverses façons dans nombre de décisions publiées. Il est toutefois possible de dégager la règle générale suivante de ces décisions : le chemin doit être tenu dans un état raisonnable d'entretien, de façon que ceux qui doivent l'emprunter puissent, en prenant des précautions normales, y circuler en sécurité. La question de savoir en quoi consiste un état raisonnable d'entretien est une question de fait, qui est fonction de toutes

by which to determine another case where the facts are different . . . .

However, we differ from the views of our colleague in that we find that the trial judge applied the correct test in determining that the municipality did not meet its standard of care, and thus did not commit an error of law of the type mentioned in *Southam*, *supra*. The trial judge applied all the elements of the *Partridge* standard to the facts, and her conclusion that the respondent municipality failed to meet this standard should not be overturned absent palpable and overriding error.

B. *The Trial Judge Did Not Commit an Error of Law*

39 We note that our colleague bases his conclusion that the municipality met its standard of care on his finding that the trial judge neglected to consider the conduct of the ordinary motorist, and thus failed to apply the correct standard of care, an error of law, which justifies his reconsideration of the evidence (para. 114). As a starting point to the discussion of the ordinary or reasonable motorist, we emphasize that the failure to discuss a relevant factor in depth, or even at all, is not itself a sufficient basis for an appellate court to reconsider the evidence. This was made clear by the recent decision of *Van de Perre*, *supra*, where Bastarache J. says, at para. 15:

. . . omissions in the reasons will not necessarily mean that the appellate court has jurisdiction to review the evidence heard at trial. As stated in *Van Mol (Guardian ad Litem of) v. Ashmore* (1999), 168 D.L.R. (4th) 637 (B.C.C.A.), leave to appeal refused [2000] 1 S.C.R. vi, an omission is only a material error if it gives rise to the reasoned belief that the trial judge must have forgotten, ignored or misconceived the evidence in a way that affected his conclusion. Without this reasoned belief, the appellate court cannot reconsider the evidence.

les circonstances de l'espèce; le terme « entretien » est une notion relative et, par conséquent, les faits propres à une affaire donnée ne permettent pas de dégager de règle déterminée permettant de trancher une autre affaire présentant des circonstances différentes . . .

Toutefois, contrairement à notre collègue, nous estimons que la juge de première instance a appliqué le bon critère juridique en concluant que la municipalité n'avait pas respecté la norme de diligence à laquelle elle était tenue, et que la juge n'a donc pas commis une erreur de droit du genre de celle décrite dans l'arrêt *Southam*, précité. La juge de première instance a appliqué aux faits de l'espèce tous les éléments du critère énoncé dans l'arrêt *Partridge*, et sa conclusion que la municipalité défenderesse n'a pas respecté ce critère ne devrait pas être infirmée en l'absence d'erreur manifeste et dominante.

B. *La juge de première instance n'a pas commis d'erreur de droit*

Nous soulignons que notre collègue fonde sa décision que la municipalité a respecté la norme de diligence sur sa conclusion que la juge de première instance a négligé de prendre en compte le comportement de l'automobiliste moyen et n'a donc pas appliqué la bonne norme de diligence, commettant ainsi une erreur de droit le justifiant de réexaminer la preuve (par. 114). Pour les besoins de l'analyse du critère de l'automobiliste moyen ou raisonnable, nous tenons au départ à signaler que l'omission d'examiner en profondeur un facteur pertinent, voire de ne pas l'examiner du tout, n'est pas en soi un fondement suffisant pour justifier une cour d'appel de réexaminer la preuve. Ce principe a été clairement énoncé dans l'arrêt récent *Van de Perre*, précité, où le juge Bastarache a dit ceci, au par. 15 :

. . . des omissions dans les motifs ne signifieront pas nécessairement que la cour d'appel a compétence pour examiner la preuve entendue au procès. Comme le dit l'arrêt *Van Mol (Guardian ad Litem of) c. Ashmore* (1999), 168 D.L.R. (4th) 637 (C.A.C.-B.), autorisation d'appel refusée [2000] 1 R.C.S. vi, une omission ne constitue une erreur importante que si elle donne lieu à la conviction rationnelle que le juge de première instance doit avoir oublié, négligé d'examiner ou mal interprété la preuve de telle manière que sa conclusion en a été affectée. Faute d'une telle conviction rationnelle, la cour d'appel ne peut pas réexaminer la preuve.

In our view, as we will now discuss, there can be no reasoned belief in this case that the trial judge forgot, ignored, or misconceived the question of the ordinary driver. It would thus be an error to engage in a re-assessment of the evidence on this issue.

The fact that the conduct of the ordinary motorist was in the mind of the trial judge from the outset is clear from the fact that she began her standard of care discussion by stating the correct test, quoting the above passage from *Partridge*, *supra*. Absent some clear sign that she subsequently varied her approach, this initial acknowledgment of the correct legal standard is a strong indication that this was the standard she applied. Not only is there no indication that she departed from the stated test, but there are further signs which support the conclusion that the trial judge applied the *Partridge* standard. The first such indication is that the trial judge did discuss, both explicitly and implicitly, the conduct of an ordinary or reasonable motorist approaching the curve. The second indication is that she referred to the evidence of the experts, Mr. Anderson and Mr. Werner, both of whom discussed the conduct of an ordinary motorist in this situation. Finally, the fact that the trial judge apportioned negligence to Mr. Nikolaisen indicates that she assessed his conduct against the standard of the ordinary driver, and thus considered the conduct of the latter.

The discussion of the ordinary motorist is found in the passage from the trial judgment immediately following the statement of the requisite standard of care:

> Snake Hill Road is a low traffic road. It is however maintained by the R.M. so that it is passable year round. There are permanent residences on the road. It is used by farmers for access to their fields and cattle. Young people frequent Snake Hill Road for parties and as such the road is used by those who may not have the same degree of familiarity with it as do residents.

À notre avis, comme nous allons le voir, la présente espèce ne peut faire naître la conviction rationnelle que la juge de première instance a oublié d'examiner la question du conducteur moyen, en a fait abstraction ou l'a mal interprétée. Il serait donc erroné de réexaminer la preuve relative à cette question.

40 Le fait que, dès le départ, la juge de première instance a eu à l'esprit la conduite de l'automobiliste moyen ressort clairement du fait qu'elle a commencé son examen de la norme de diligence en formulant le critère approprié, c'est-à-dire en citant le passage susmentionné de l'arrêt *Partridge*, précité. En l'absence d'indications claires qu'elle a subséquemment modifié sa méthode d'analyse, cette mention initiale de la norme juridique appropriée constitue un indice solide qu'il s'agit bien de la norme qu'elle a appliquée. Non seulement rien n'indique qu'elle s'est écartée du critère énoncé, mais d'autres indices étayent la conclusion qu'elle a appliqué le critère de l'arrêt *Partridge*. Le premier de ces indices est que la juge s'est bel et bien interrogée, tant explicitement qu'implicitement, sur la conduite de l'automobiliste moyen ou raisonnable s'approchant du virage. Le deuxième indice est qu'elle a fait état des témoignages des experts, MM. Anderson et Werner, qui ont tous deux analysé le comportement de l'automobiliste moyen se trouvant dans cette situation. Enfin, le fait que la juge de première instance ait imputé une partie de la responsabilité à M. Nikolaisen indique qu'elle a évalué sa conduite eu égard au critère du conducteur moyen, et qu'elle a donc pris en compte la conduite de ce dernier.

41 On trouve l'analyse relative à l'automobiliste moyen dans cet extrait du jugement de première instance qui suit immédiatement l'énoncé de la norme de diligence requise :

> [TRADUCTION] Le chemin Snake Hill est un chemin à faible débit de circulation. Il est néanmoins entretenu par la M.R. à longueur d'année afin de le garder carrossable. Des résidences permanentes sont situées en bordure de celui-ci. Les fermiers l'utilisent pour accéder à leurs champs et à leur bétail. Des jeunes gens empruntent le chemin Snake Hill pour se rendre à des fêtes, de sorte qu'il est utilisé par des conducteurs qui ne le connaissent pas toujours aussi bien que les résidents de l'endroit.

There is a portion of Snake Hill Road that is a hazard to the public. In this regard I accept the evidence of Mr. Anderson and Mr. Werner. Further, it is a hazard that is not readily apparent to users of the road. It is a hidden hazard. The location of the Nikolaisen rollover is the most dangerous segment of Snake Hill Road. Approaching the location of the Nikolaisen rollover, limited sight distance, created by uncleared bush, precludes a motorist from being forewarned of an impending sharp right turn immediately followed by a left turn. While there were differing opinions on the *maximum* speed at which this curve can be negotiated, I am satisfied that when limited sight distance is combined with the tight radius of the curve and lack of superelevation, this curve cannot be *safely* negotiated at speeds greater than 60 kilometres per hour when conditions are favourable, or 50 kilometres per hour when wet.

. . . where the existence of that bush obstructs the ability of a motorist to be forewarned of a hazard such as that on Snake Hill Road, it is reasonable to expect the R.M. to erect and maintain a warning or regulatory sign so that a motorist, using ordinary care, may be forewarned, adjust speed and take corrective action in advance of entering a dangerous situation. [Underlining added; italics in original.]

([1998] 5 W.W.R. 523, at paras. 84-86)

42 In our view, this passage indicates that the trial judge did consider how a motorist exercising ordinary care would approach the curve in question. The implication of labelling the curve a "hidden hazard" which is "not readily apparent to users of the road", is that the danger is of the type that cannot be anticipated. This in turn implies that, even if the motorist exercises ordinary care, he or she will not be able to react to the curve. As well, the trial judge referred explicitly to the conduct of a motorist exercising ordinary care: "it is reasonable to expect the R.M. to erect and maintain a warning or regulatory sign so that a motorist, using ordinary care, may be forewarned, adjust speed and take corrective action in advance of entering a dangerous situation" (para. 86 (emphasis added)).

Il y a, sur le chemin Snake Hill, un tronçon qui présente un danger pour le public. À cet égard, je retiens les témoignages de MM. Anderson et Werner. En outre, il s'agit d'un danger qui n'est pas facilement décelable par les usagers du chemin. Il s'agit d'un danger caché. L'endroit où le véhicule de M. Nikolaisen a fait un tonneau est situé sur le tronçon le plus dangereux du chemin Snake Hill. À l'approche de cet endroit, des broussailles réduisent la distance de visibilité de l'automobiliste et l'empêchent de voir l'imminence d'un virage à droite serré, qui est immédiatement suivi d'un virage à gauche. Bien que des opinions divergentes aient été émises quant à la vitesse *maximale* à laquelle ce virage peut être pris, je suis d'avis que, vu la distance de visibilité réduite, l'existence d'une courbe serrée et l'absence de surélévation du chemin, ce virage ne peut être pris *en sécurité* à une vitesse supérieure à 60 kilomètres à l'heure dans des conditions favorables, ou 50 kilomètres à l'heure sur chaussée humide.

. . . à l'endroit où la présence des broussailles empêche les automobilistes de voir venir un danger comme celui qui existe sur le chemin Snake Hill, il est raisonnable de s'attendre à ce que la M.R. installe et maintienne un panneau d'avertissement ou de signalisation afin qu'un automobiliste prenant des précautions normales soit prévenu et puisse réduire sa vitesse et prendre des mesures correctives avant d'arriver à l'endroit dangereux. [Nous soulignons; en italique dans l'original.]

([1998] 5 W.W.R. 523, par. 84-86)

À notre avis, cet extrait indique que la juge de première instance a effectivement pris en compte la façon dont l'automobiliste prenant des précautions normales s'approcherait du virage en question. Qualifier le virage de [TRADUCTION] « danger caché », danger qui « n'est pas facilement décelable par les usagers du chemin », implique que le danger en est un qu'il est impossible de prévoir. Il s'ensuit que, même si l'automobiliste prend des précautions normales, il ne pourra pas réagir à la présence du virage. Par ailleurs, la juge de première instance a explicitement fait état de la conduite de l'automobiliste prenant des précautions normales : [TRADUCTION] « [I]l est raisonnable de s'attendre à ce que la M.R. installe et maintienne un panneau d'avertissement ou de signalisation afin qu'un automobiliste prenant des précautions normales soit prévenu et puisse réduire sa vitesse et prendre des mesures correctives avant d'arriver à l'endroit dangereux » (par. 86 (nous soulignons)).

With respect to the speed of a motorist approaching the curve, there is also an indication that the trial judge considered the conduct of an ordinary motorist. First, she stated that she accepted the evidence of Mr. Anderson and Mr. Werner with respect to the finding that the curve constituted a hazard to the public. The evidence given by these experts suggests that between 60 and 80 km/h is a reasonable speed to drive parts of this road, and at that speed, the curve presents a hazard. Their evidence also indicates their general opinion that the curve was a hazardous one. Mr. Anderson refers to the curve being difficult to negotiate at "normal speeds". Also, Mr. Anderson states that "if you're not aware that this curve is there, the sharp course of the curve, and you enter too far into it before you realize that the curve is there, then you have to do a tighter radius than 118 metres in order to get back on track to be able to negotiate the second curve". He also states that "you could be lulled into thinking you've got an 80 kilometres an hour road until you are too far into the tight curve to be able to respond".

43 Relativement à la vitesse à laquelle les automobilistes s'approchent du virage, il existe également un indice confirmant que la juge de première instance a pris en compte la conduite de l'automobiliste moyen. Premièrement, elle a dit qu'elle acceptait les témoignages de MM. Anderson et de Werner en ce qui concerne la conclusion que la courbe constituait un danger pour le public. Leurs témoignages suggèrent qu'une vitesse de 60 à 80 km/h est une vitesse raisonnable à certains endroits de ce chemin et que, à cette vitesse, la courbe constitue un danger. Leurs témoignages indiquent également qu'ils estiment de façon générale que la courbe est dangereuse. De dire M. Anderson, le virage est difficile à prendre à des [TRADUCTION] « vitesses normales ». Il ajoute que, [TRADUCTION] « si on ne connaît pas la présence de ce virage à cet endroit, le caractère prononcé du virage, et qu'on ne s'aperçoit pas qu'il y a un virage avant de s'être déjà engagé trop loin dans celui-ci, il faut tourner dans un rayon inférieur à 118 mètres pour corriger sa trajectoire afin d'être en mesure de prendre le deuxième virage ». Il affirme également qu' [TRADUCTION] « on peut être amené à croire qu'on se trouve sur une route où il est possible de rouler à 80 km/h, jusqu'à ce qu'on soit engagé trop loin dans le virage serré pour être capable de réagir ».

The Court of Appeal found that, given the nature and condition of Snake Hill Road, the contention that this rural road would be taken at 80 km/h by the ordinary motorist was untenable. However, it is clear from the trial judge's reasons that she did not take 80 km/h as the speed at which the ordinary motorist would approach the curve. Instead she found, based on expert evidence, that "this curve cannot be *safely* negotiated at speeds greater than 60 kilometres per hour when conditions are favourable, or 50 kilometres per hour when wet" (para. 85 (emphasis in original)). From this finding, coupled with the finding that the curve was hidden and unexpected, the logical conclusion is that the trial judge found that a motorist exercising ordinary care could easily be deceived into approaching the curve at speeds in excess of the safe speed for the curve, and subsequently be taken by surprise. Therefore, the trial judge found that the curve was hazardous to the ordinary

44 La Cour d'appel a jugé que, vu la nature et l'état du chemin Snake Hill, la prétention selon laquelle l'automobiliste moyen roulerait sur cette route rurale à 80 km/h était insoutenable. Toutefois, il ressort clairement des motifs de la juge de première instance qu'elle ne considérait pas que l'automobiliste moyen s'approcherait du virage à 80 km/h. Elle a plutôt conclu, à partir des témoignages des experts, que [TRADUCTION] « ce virage ne peut être pris *en sécurité* à une vitesse supérieure à 60 kilomètres à l'heure dans des conditions favorables, ou 50 kilomètres à l'heure sur chaussée humide » (par. 85 (en italique dans l'original)). De cette constatation, conjuguée à celle que le virage était caché et imprévu, il est logique de conclure que la juge de première instance a estimé que l'automobiliste prenant des précautions normales pouvait aisément être amené à s'approcher du virage à des vitesses supérieures à la vitesse sécuritaire pour le prendre, et se retrouver ensuite pris au dépourvu. La juge de première

motorist and it follows that she applied the correct standard of care.

45 In our respectful view, our colleague errs in agreeing with the Court of Appeal's finding that the trial judge should have addressed the conduct of the ordinary motorist more fully (para. 124). At para. 119, he writes:

> A proper application of the test demands that the trial judge ask the question: "How would a reasonable driver have driven on this road?" Whether or not a hazard is "hidden" or a curve is "inherently" dangerous does not dispose of the question.

And later, he states, "In my view, the question of how the reasonable driver would have negotiated Snake Hill Road necessitated a somewhat more in-depth analysis of the character of the road" (para. 125). With respect, requiring the trial judge to have made this specific inquiry in her reasons is inconsistent with *Van de Perre*, *supra*, which makes it clear that an omission or a failure to discuss a factor in depth is not, in and of itself, a basis for interfering with the findings of the trial judge and reweighing the evidence. As we note above, it is clear that although the trial judge may not have conducted an extensive review of this element of the *Partridge* test, she did indeed consider this factor by stating the correct test, then applying this test to the facts.

46 We note that in relying on the evidence of Mr. Anderson and Mr. Werner, the trial judge chose not to base her decision on the conflicting evidence of other witnesses. However, her reliance on the evidence of Mr. Anderson and Mr. Werner is insufficient proof that she "forgot, ignored, or misconceived" the evidence. The full record was before the trial judge and we can presume that she reviewed all of it, absent further proof that the trial judge forgot, ignored or misapprehended the evidence, leading to an error in law. It is open to a trial judge to prefer the evidence of some witnesses over others:

instance a donc conclu que le virage était dangereux pour l'automobiliste moyen et il s'ensuit qu'elle a appliqué la norme de diligence appropriée.

En toute déférence, notre collègue commet une erreur en souscrivant à la conclusion de la Cour d'appel selon laquelle la juge de première instance aurait dû examiner de manière plus approfondie la conduite de l'automobiliste moyen (par. 124). Il écrit ceci, au par. 119 :

> Pour bien appliquer le critère juridique, le juge de première instance doit se poser la question suivante : « Comment un conducteur raisonnable aurait-il roulé sur ce chemin? » Le fait de conclure qu'il existe ou non un danger « caché » ou qu'une courbe est quelque chose d'« intrinsèquement » dangereux ne vide pas la question.

Plus loin, il dit : « À mon avis, la question de savoir comment un conducteur raisonnable aurait roulé sur le chemin Snake Hill nécessitait un examen un peu plus approfondi de la nature du chemin » (par. 125). En toute déférence, considérer que la juge de première instance aurait dû faire cette analyse particulière dans ses motifs est incompatible avec l'arrêt *Van de Perre*, précité, lequel établit clairement que l'omission ou le défaut d'analyser un facteur en profondeur ne constitue pas, en soi, une raison justifiant de modifier les conclusions du juge de première instance et de réexaminer la preuve. Comme nous l'avons dit précédemment, il est clair que, quoique la juge de première instance n'ait peut-être pas fait une analyse approfondie de ce volet du critère énoncé dans l'arrêt *Partridge*, elle a effectivement tenu compte de ce facteur en formulant le critère approprié puis en l'appliquant aux faits de l'espèce.

Nous tenons à souligner que, en s'appuyant sur les témoignages de MM. Anderson et Werner, la juge de première instance a choisi de ne pas fonder sa décision sur les témoignages contradictoires rendus par d'autres témoins. Toutefois, cela ne suffit pas pour établir qu'elle a « oublié, négligé d'examiner ou mal interprété » la preuve. La juge de première instance disposait de l'ensemble du dossier et on peut présumer qu'elle l'a étudié d'un bout à l'autre, en l'absence d'autre indication qu'elle a oublié, négligé d'examiner ou mal interprété la preuve, commettant ainsi une erreur de droit. Le juge de première

Toneguzzo-Norvell, *supra*, at p. 123. Mere reliance by the trial judge on the evidence of some witnesses over others cannot on its own form the basis of a "reasoned belief that the trial judge must have forgotten, ignored or misconceived the evidence in a way that affected his conclusion" (*Van de Perre*, *supra*, at para. 15). This is in keeping with the narrow scope of review by an appellate court applicable in this case.

A further indication that the trial judge considered the conduct of an ordinary motorist on Snake Hill Road is her finding that both Mr. Nikolaisen and the municipality breached their duty of care to Mr. Housen, and that the defendant Nikolaisen was 50 percent contributorily negligent. Since a finding of negligence implies a failure to meet the ordinary standard of care, and since Mr. Nikolaisen's negligence related to his driving on the curve, to find that Mr. Nikolaisen's conduct on the curve failed to meet the standard of the ordinary driver implies a consideration of that ordinary driver on the curve. The fact that the trial judge distinguished the conduct of Mr. Nikolaisen in driving negligently on the road from the conduct of the municipality in negligently failing to erect a warning sign is evidence that the trial judge kept the municipality's legal standard clearly in mind in its application to the facts, and that she applied this standard to the ordinary driver, not the negligent driver.

To summarize, in the course of her reasons, the trial judge first stated the requisite standard of care from *Partridge*, *supra*, relating to the conduct of the ordinary driver. She then applied that standard to the facts referring again to the conduct of the ordinary driver. Finally, in light of her finding that the municipality breached this standard, she apportioned negligence between the driver and the municipality in a way which again entailed a consideration of the

instance peut retenir la déposition de certains témoins de préférence à d'autres : *Toneguzzo-Norvell*, précité, p. 123. Le fait pour le juge de première instance de s'appuyer sur certains témoignages plutôt que sur d'autres ne peut à lui seul fournir l'assise d'une « conviction rationnelle que le juge de première instance doit avoir oublié, négligé d'examiner ou mal interprété la preuve de telle manière que sa conclusion en a été affectée » (*Van de Perre*, précité, par. 15). Cette conclusion est compatible avec la portée restreinte de l'examen qu'il convient de faire en appel dans la présente affaire.

47 Une autre indication que la juge de première instance s'est interrogée sur la façon dont conduit l'automobiliste moyen sur le chemin Snake Hill est sa conclusion que M. Nikolaisen et la municipalité ont tous deux manqué à leur obligation de diligence envers M. Housen, et que le défendeur Nikolaisen était responsable de négligence concourante dans une proportion de 50 p. 100. Comme une conclusion de négligence implique un manquement à la norme de diligence habituelle, et comme la négligence de M. Nikolaisen était liée à sa manière de conduire dans le virage, la conclusion que sa conduite à cet endroit ne respectait pas le critère du conducteur moyen suppose qu'on s'est demandé comment ce conducteur s'approcherait du virage. La distinction qu'a établie la juge de première instance entre la négligence dont a fait preuve M. Nikolaisen lorsqu'il roulait sur le chemin et celle dont la municipalité a fait montre en omettant d'installer un panneau d'avertissement prouve qu'elle n'a pas perdu de vue la norme juridique régissant la municipalité et l'application de cette norme aux faits, et que la juge a appliqué cette norme au conducteur moyen, et non au conducteur négligent.

48 En résumé, dans ses motifs la juge de première instance a d'abord énoncé la norme de diligence requise par l'arrêt *Partridge*, précité, relativement à la conduite de l'automobiliste moyen. Elle a ensuite appliqué cette norme aux faits, se reportant encore une fois à la conduite de l'automobiliste moyen. Enfin, vu sa conclusion que la municipalité avait manqué à cette norme de diligence, elle a réparti la responsabilité entre le conducteur

ordinary driver. As such, we are overwhelmingly drawn to the conclusion that the conduct of the ordinary driver was both considered and applied by the trial judge.

49 Thus, we conclude that the trial judge did not commit an error of law with respect to the municipality's standard of care. On this matter, we disagree with the basis for the re-assessment of the evidence undertaken by our colleague (paras. 122-42) and regard this re-assessment to be an unjustified intrusion into the finding of the trial judge that the municipality breached its standard of care. This finding is a question of mixed law and fact which should not be overturned absent a palpable and overriding error. As discussed below, it is our view that no such error exists, as the trial judge conducted a reasonable assessment based on her view of the evidence.

C. *The Trial Judge Did Not Commit A Palpable or Overriding Error*

50 Despite this high standard of review, the Court of Appeal found that a palpable and overriding error was made by the trial judge ([2000] 4 W.W.R. 173, 2000 SKCA 12, at para. 84). With respect, this finding was based on the erroneous presumption that the trial judge accepted 80 km/h as the speed at which an ordinary motorist would approach the curve, a presumption which our colleague also adopts in his reasons (para. 133).

51 As discussed above, the trial judge's finding was that an ordinary motorist could approach the curve in excess of 60 km/h in dry conditions, and 50 km/h in wet conditions, and that at such speeds the curve was hazardous. The trial judge's finding was not based on a particular speed at which the curve would be approached by the ordinary motorist. Instead, she found that, because the curve was hidden and sharper than would be anticipated, a motorist exercising ordinary care could approach it at greater than

et la municipalité d'une manière qui, une fois de plus, atteste la prise en compte du critère du conducteur moyen. En conséquence, nous en venons irrésistiblement à la conclusion que la juge de première instance a pris en compte et appliqué ce critère.

Par conséquent, nous estimons que la juge de première instance n'a pas commis d'erreur de droit en ce qui concerne la norme de diligence à laquelle était tenue la municipalité. Sur ce point, nous ne souscrivons pas aux raisons sur lesquelles se fondent notre collègue pour réexaminer la preuve (aux par. 122 à 142) et nous considérons ce réexamen comme une intervention injustifiée relativement à la conclusion de la juge de première instance portant que la municipalité a manqué à la norme de diligence à laquelle elle était tenue. Cette conclusion porte sur une question mixte de droit et de fait et elle ne peut pas être infirmée en l'absence d'erreur manifeste et dominante. Comme nous le verrons plus loin, nous sommes d'avis qu'aucune erreur de cette nature n'a été commise, car la juge de première instance a fait une analyse raisonnable, fondée sur son appréciation de la preuve.

C. *La juge de première instance n'a pas commis d'erreur manifeste ou dominante*

Malgré cette norme de contrôle sévère, la Cour d'appel a jugé que la juge de première instance avait commis une erreur manifeste et dominante ([2000] 4 W.W.R. 173, 2000 SKCA 12, par. 84). En toute déférence, cette conclusion repose sur la présomption erronée selon laquelle la juge aurait accepté que l'automobiliste moyen approcherait du virage à 80 km/h, présomption qu'adopte également notre collègue dans ses motifs (par. 133).

Comme nous l'avons vu plus tôt, la conclusion de la juge de première instance était que l'automobiliste moyen pourrait s'approcher du virage à une vitesse supérieure à 60 km/h sur chaussée sèche, et 50 km/h sur chaussée humide, mais qu'à ces vitesses le virage était dangereux. Cette conclusion n'était pas fondée sur une vitesse précise à laquelle l'automobiliste moyen s'approcherait du virage. La juge de première instance a plutôt estimé que, parce que le virage est caché et plus serré que ce à quoi on

the speed at which it would be safe to negotiate the curve.

As we explain in greater detail below, in our opinion, not only is this assessment far from reaching the level of a palpable and overriding error, in our view, it is a sensible and logical way to deal with large quantities of conflicting evidence. It would be unrealistic to focus on some exact speed at which the curve would likely be approached by the ordinary motorist. The findings of the trial judge in this regard were the result of a reasonable and practical assessment of the evidence as a whole.

In finding a palpable and overriding error, Cameron J.A. relied on the fact that the trial judge adopted the expert evidence of Mr. Anderson and Mr. Werner which was premised on a *de facto* speed limit of 80 km/h taken from *The Highway Traffic Act*, S.S. 1986, c. H-3.1. However, whether or not the experts based their testimony on this limit, the trial judge did not adopt that limit as the speed of the ordinary motorist approaching the curve. Again, the trial judge found that the curve could not be taken safely at greater than 60 km/h dry and 50 km/h wet, and there is evidence in the record to support this finding. For example, Mr. Anderson states:

If you don't anticipate the curve and you get too far into it before you start to do your correction then you can get into trouble even at, probably at 60. Fifty you'd have to be a long ways into it, but certainly at 60 you could.

It is notable too that both Mr. Anderson and Mr. Werner would have recommended installing a sign, warning motorists of the curve, with a posted limit of 50 km/h.

Although clearly the curve could not be negotiated safely at 80 km/h, it could also not be

s'attend normalement, il était possible qu'un automobiliste prenant des précautions normales s'en approche à une vitesse supérieure à la vitesse sécuritaire pour prendre le virage.

52 Comme nous allons le préciser plus loin, nous sommes d'avis que non seulement cette appréciation est-elle loin de constituer une erreur manifeste et dominante, mais elle est une réponse judicieuse et logique eu égard à l'abondance d'éléments de preuve contradictoires. Il serait irréaliste de fixer une quelconque vitesse à laquelle l'automobiliste moyen s'approcherait vraisemblablement du virage. Les conclusions de la juge de première instance à cet égard découlent d'une évaluation raisonnable et réaliste de l'ensemble de la preuve.

53 En concluant à l'existence d'une erreur manifeste et dominante, le juge Cameron de la Cour d'appel s'est appuyé sur le fait que la juge de première instance avait retenu les témoignages d'expert de MM. Anderson et Werner, lesquels étaient fondés sur la vitesse limite *de facto* de 80 km/h prévue par la *Highway Traffic Act*, S.S. 1986, ch. H-3.1. Toutefois, que le témoignage des experts ait été ou non fondé sur cette limite, la juge de première instance n'a pas retenu cette vitesse comme étant celle à laquelle l'automobiliste moyen s'approche du virage. Rappelons que la juge de première instance a estimé qu'il n'était pas possible d'aborder le virage en sécurité à une vitesse supérieure à 60 km/h sur chaussée sèche et 50 km/h sur chaussée humide, et il existe au dossier des éléments étayant cette conclusion. Par exemple, M. Anderson a dit ceci :

[TRADUCTION] Si vous ne prévoyez pas l'arrivée du virage et que vous vous engagez trop loin dans celui-ci avant d'amorcer votre manœuvre correctrice, vous risquez d'avoir des ennuis même à, probablement à 60. À cinquante il faudrait que vous soyez engagé assez loin, mais à 60 vous pourriez certainement en avoir.

Il convient également de signaler que MM. Anderson et Werner auraient tous deux recommandé l'installation d'un panneau avertissant les automobilistes de l'imminence du virage et fixé la vitesse maximale permise à 50 km/h.

54 Le virage ne pouvait manifestement pas être pris en sécurité à 80 km/h, mais il ne pouvait l'être non

negotiated safely at much slower speeds. It should also be noted that the trial judge did not adopt the expert testimony of Mr. Anderson and Mr. Werner in its entirety. She stated: "There is a portion of Snake Hill Road that is a hazard to the public. In this regard I accept the evidence of Mr. Anderson and Mr. Werner" (para. 85 (emphasis added)). It cannot be assumed from this that she accepted a *de facto* speed limit of 80 km/h especially when one bears in mind (1) the trial judge's statement of the safe speeds of 50 and 60 km/h, and (2) the fact that both these experts found the road to be unsafe at much lower speeds than 80 km/h.

55 Given that the trial judge did not base her standard of care analysis on a *de facto* speed limit of 80 km/h, it then follows that the Court of Appeal's finding of a palpable and overriding error cannot stand.

56 Furthermore, the narrowly defined scope of appellate review dictates that a trial judge should not be found to have misapprehended or ignored evidence, or come to the wrong conclusions merely because the appellate court diverges in the inferences it draws from the evidence and chooses to emphasize some portions of the evidence over others. As we are of the view that the trial judge committed no error of law in finding that the municipality breached its standard of care, we are also respectfully of the view that our colleague's re-assessment of the evidence on this issue (paras. 129-42) is an unjustified interference with the findings of the trial judge, based on a difference of opinion concerning the inferences to be drawn from the evidence and the proper weight to be placed on different portions of the evidence. For instance, in the opinion of our colleague, based on some portions of the expert evidence, a reasonable driver exercising ordinary care would approach a rural road at 50 km/h or less, because a reasonable driver would have difficulty seeing the sharp radius of the curve and oncoming traffic (para. 129). However, the trial judge, basing her assessment on other portions of the expert evidence, found that the nature of the road was such that a motorist could be

plus à des vitesses beaucoup plus réduites. Il convient également de souligner que la juge de première instance n'a pas retenu intégralement les témoignages d'expert de MM. Anderson et Werner. Elle a dit : [TRADUCTION] « Il y a, sur le chemin Snake Hill, un tronçon qui présente un danger pour le public. À cet égard, je retiens les témoignages de MM. Anderson et Werner » (par. 85 (nous soulignons)). Ces propos ne permettent pas de présumer qu'elle acceptait une vitesse limite *de facto* de 80 km/h, particulièrement si l'on se rappelle (1) qu'elle a dit qu'on pouvait rouler en sécurité à des vitesses de 50 et de 60 km/h, et (2) que ces deux experts ont considéré que le chemin n'était pas sûr même à des vitesses bien inférieures à 80 km/h.

Puisque la juge de première instance n'a pas fondé son analyse de la norme de diligence sur une vitesse limite *de facto* de 80 km/h, il s'ensuit que la conclusion de la Cour d'appel relativement à l'existence d'une erreur manifeste et dominante ne saurait être confirmée.

En outre, vu la portée restreinte de la révision en appel, on ne saurait conclure qu'un juge de première instance a négligé d'examiner la preuve, l'a mal interprétée ou est arrivé à des conclusions erronées, simplement parce que le tribunal d'appel tire des inférences divergentes de la preuve et décide d'accorder plus d'importance à certains éléments qu'à d'autres. Étant d'avis que la juge de première instance n'a pas commis d'erreur de droit en concluant que la municipalité avait violé la norme de diligence à laquelle elle était tenue, nous estimons aussi, en toute déférence, que le réexamen de la preuve auquel procède notre collègue sur cette question (aux par. 129 à 142) constitue une intervention injustifiée relativement aux conclusions de la juge de première instance, fondée sur une divergence d'opinions quant aux inférences devant être tirées de la preuve et au poids qu'il convient d'accorder à divers éléments. Par exemple, notre collègue est d'avis, sur la foi de certaines parties des témoignages d'expert, qu'un conducteur raisonnable prenant des précautions normales roulerait sur une route rurale à une vitesse maximale de 50 km/h, parce qu'il aurait de la difficulté à voir que le virage est serré et s'il vient des véhicules en sens inverse (par. 129). Or, se

deceived into believing that the road did not contain a sharp curve and thus would approach the road normally, unaware of the hidden danger.

We are faced in this case with conflicting expert evidence on the issue of the correct speed at which an ordinary motorist would approach the curve on Snake Hill Road. The differing inferences from the evidence drawn by the trial judge and the Court of Appeal amount to a divergence on what weight should be placed on various pieces of conflicting evidence. As noted by our colleague, Mr. Sparks was of the opinion that "[if] you can't see around the corner, then, you know, drivers would have a fairly strong signal . . . that due care and caution would be required". Similar evidence of this nature was given by Mr. Nikolaisen, and indeed even by Mr. Anderson and Mr. Werner. This is contrasted with evidence such as that given by Mr. Anderson and Mr. Werner that a reasonable driver would be "lulled" into thinking that there is an 80 km/h road ahead of him or her.

As noted by McLachlin J. in *Toneguzzo-Norvell*, *supra*, at p. 122 and mentioned above, "the weight to be assigned to the various pieces of evidence is under our trial system essentially the province of the trier of fact". In that case, a unanimous Court found that the Court of Appeal erred in interfering with the trial judge's factual findings, on the basis that it was open to the trial judge to place less weight on certain evidence and accept other, conflicting evidence which the trial judge found to be more convincing (*Toneguzzo-Norvell*, at pp. 122-23). Similarly, in this case, the trial judge's factual findings concerning the proper speed to be used on approaching the curve should not be interfered with. It was open to her to choose to place more weight on certain portions of the evidence of Mr. Anderson and Mr. Werner, where the evidence was conflicting. Her assessment of the proper speed was a reasonable inference based on the evidence and does not reach

fondant sur d'autres parties des témoignages d'expert, la juge de première instance a estimé que la nature du chemin était telle qu'un automobiliste pourrait être amené à croire que le chemin ne comporte pas de virage serré et, de ce fait, à y rouler normalement, sans soupçonner l'existence du danger caché.

57 En l'espèce, nous sommes en présence de témoignages d'expert contradictoires sur la question de la vitesse à laquelle l'automobiliste moyen s'approcherait du virage du chemin Snake Hill. Les inférences différentes que la juge de première instance et la Cour d'appel tirent de la preuve équivalent à une divergence d'opinion quant au poids à accorder à divers éléments de preuve contradictoires. Le témoin Sparks a émis l'opinion suivante, que cite également notre collègue : [TRADUCTION] « [Si] vous ne pouvez voir, de l'autre côté du virage, alors, vous savez, cela devrait envoyer un message clair aux conducteurs [. . .] que l'attention et la prudence s'imposent ». M. Nikolaisen, et même MM. Anderson et Werner ont d'ailleurs témoigné au même effet. Cela contraste avec l'affirmation de MM. Anderson et Werner selon laquelle un conducteur raisonnable serait [TRADUCTION] « amené » à croire qu'il se trouve sur un chemin où l'on peut rouler à 80 km/h.

58 Comme l'a souligné madame le juge McLachlin, à la p. 122 de l'arrêt *Toneguzzo-Norvell*, précité, « selon notre système de procès, il appartient essentiellement au juge des faits [. . .] d'attribuer un poids aux différents éléments de preuve ». Dans cette affaire, notre Cour a conclu à l'unanimité que la Cour d'appel avait commis une erreur en modifiant les conclusions de fait du juge de première instance, au motif qu'il était loisible à celui-ci d'accorder un poids moins grand à certains éléments de preuve et à accepter d'autres éléments contradictoires, qu'il considérait plus convaincants. (*Toneguzzo-Norvell*, p. 122-123). De même, en l'espèce, il n'y a pas lieu de modifier les conclusions de fait de la juge de première instance au sujet de la vitesse à laquelle il faudrait approcher du virage. Il lui était loisible d'accorder plus de poids à certaines parties des témoignages de MM. Anderson et Werner, dans les cas où la preuve était contradictoire. Son

the level of a palpable and overriding error. As such, the trial judge's findings with respect to the standard of care should not be overturned.

IV. Knowledge of the Municipality

59 We agree with our colleague that s. 192(3) of *The Rural Municipality Act*, *1989*, requires the plaintiff to show that the municipality knew or should have known of the disrepair of Snake Hill Road before the municipality can be found to have breached its duty of care under s. 192. We also agree that the evidence of the prior accidents, in and of itself, is insufficient to impute such knowledge to the municipality. However, we find that the trial judge did not err in her finding that the municipality knew or ought to have known of the disrepair.

60 As discussed, the question of whether the municipality knew or should have known of the disrepair of Snake Hill Road is a question of mixed fact and law. The issue is legal in the sense that the municipality is held to a legal standard of knowledge of the nature of the road, and factual in the sense of whether it had the requisite knowledge on the facts of this case. As we state above, absent an isolated error in law or principle, such a finding is subject to the "palpable and overriding" standard of review. In this case, our colleague concludes that the trial judge erred in law by failing to approach the question of knowledge from the perspective of a prudent municipal councillor, and holds that a prudent municipal councillor could not be expected to become aware of the risk posed to the ordinary driver by the hazard in question. He also finds that the trial judge erred in law by failing to recognize that the burden of proving knowledge rested with the plaintiff. With respect, we disagree with these conclusions.

appréciation de la vitesse appropriée constituait une inférence raisonnable, fondée sur la preuve, et elle ne constitue pas une erreur manifeste et dominante. Dans ce contexte, il n'y a pas lieu d'écarter ses conclusions concernant la norme de diligence.

IV. Connaissance de la municipalité

À l'instar de notre collègue, nous estimons que le par. 192(3) de la *Rural Municipality Act, 1989*, oblige le demandeur à démontrer que la municipalité connaissait ou aurait dû connaître le mauvais état du chemin Snake Hill pour qu'il soit possible de conclure qu'elle a manqué à l'obligation de diligence qui lui incombe en vertu de l'art. 192. Nous sommes nous aussi d'avis que la preuve des accidents antérieurs n'est pas, en soi, suffisante pour prêter cette connaissance à la municipalité. Cependant, nous arrivons à la conclusion que la juge de première instance n'a pas commis d'erreur lorsqu'elle a conclu que la municipalité connaissait ou aurait dû connaître le mauvais état du chemin.

Comme nous l'avons vu, la question de savoir si la municipalité connaissait ou aurait dû connaître le mauvais état du chemin Snake Hill est une question mixte de droit et de fait. Il s'agit, d'une part, d'une question de droit en ce que la municipalité est tenue à une norme juridique qui lui impose de connaître la nature du chemin, et, d'autre part, d'une question de fait en ce qu'il faut déterminer si, eu égard aux faits de l'espèce, elle avait la connaissance requise. Comme nous l'avons dit précédemment, en l'absence d'erreur de droit ou de principe isolable, une telle conclusion est assujettie à la norme de contrôle de l'erreur « manifeste et dominante ». En l'espèce, notre collègue conclut que la juge de première instance a commis une erreur de droit en ne considérant pas la question de la connaissance du point de vue du conseiller municipal prudent, et il estime qu'on ne pouvait s'attendre à ce qu'un conseiller municipal prudent s'aperçoive du risque que le danger en question faisait courir au conducteur moyen. Il est également d'avis que la juge de première instance a commis une erreur de droit en ne reconnaissant pas que la charge de prouver la connaissance incombait au demandeur. En toute déférence, nous ne pouvons souscrire à ces conclusions.

The hazard in question is an unsigned and unexpected sharp curve. In our view, when a hazard is, like this one, a permanent feature of the road which has been found to present a risk to the ordinary driver, it is open to the trial judge to draw an inference, on this basis alone, that a prudent municipal councillor ought to be aware of the hazard. In support of his conclusion on the issue of knowledge, our colleague states that the municipality's knowledge is inextricably linked to the standard of care, and ties his finding on the question of knowledge to his finding that the curve did not present a hazard to the ordinary motorist (para. 149). We agree that the question of knowledge is closely linked to the standard of care, and since we find that the trial judge was correct in holding that the curve presented a hazard to the ordinary motorist, from there it was open to the trial judge to find that the municipality ought to have been aware of this hazard. We further note that as a question of mixed fact and law this finding is subject to the "palpable and overriding" standard of review. On this point, however, we restrict ourselves to situations such as the one at bar where the hazard in question is a permanent feature of the road, as opposed to a temporary hazard which reasonably may not come to the attention of the municipality in time to prevent an accident from occurring.

61 Le danger en question est une courbe serrée et soudaine, qui n'est annoncée par aucune signalisation. À notre avis, lorsqu'un danger constitue, comme celui-ci qui nous intéresse, une caractéristique permanente qui, a-t-on jugé, présente un risque pour le conducteur moyen, le juge de première instance peut, pour ce seul motif, inférer qu'un conseiller municipal prudent aurait dû connaître l'existence d'un danger. Pour étayer sa conclusion sur la question de la connaissance, notre collègue affirme que la connaissance de la municipalité est intimement liée à celle de la norme de diligence, et il lie sa conclusion sur la connaissance à sa conclusion selon laquelle la courbe ne constituait pas un danger pour l'automobiliste moyen (par. 149). Nous reconnaissons que la question de la connaissance est étroitement liée à celle de la norme de diligence, et, comme nous estimons que la juge de première instance a eu raison de conclure que la courbe présentait un danger pour l'automobiliste moyen, elle pouvait dès lors juger que la municipalité aurait dû connaître ce danger. Soulignons également que cette conclusion visant une question mixte de fait et de droit est assujettie à la norme de contrôle de l'erreur « manifeste et dominante ». Sur ce point, toutefois, nous limitons la portée de notre opinion aux situations analogues à celle qui nous occupe, où le danger constitue une caractéristique permanente du chemin, par opposition à un danger temporaire dont une municipalité pourrait raisonnablement ne pas être informée en temps utile pour empêcher un accident de survenir.

In addition, our colleague relies on the evidence of the lay witnesses, Craig and Toby Thiel, who lived on Snake Hill Road, and who testified that they had not experienced any difficulties with it (para. 149). With respect, we find three problems with this reliance. First, since the curve was found to be a hazard based on its hidden and unexpected nature, relying on the evidence of those who drive the road on a daily basis does not, in our view, assist in determining whether the curve presented a hazard to the ordinary motorist, or whether the municipality ought to have been aware of the hazard. In addition, in finding that the municipality ought to have known of the disrepair, the trial judge clearly chose not to rely on the above evidence. As we state above,

62 Par ailleurs, notre collègue se fonde sur les dépositions de témoins ordinaires, Craig et Toby Thiel, qui habitaient sur le chemin Snake Hill et qui ont témoigné n'avoir jamais éprouvé de difficulté à conduire à cet endroit (par. 149). En toute déférence, nous estimons que le fait de se fonder sur ces témoignages pose trois problèmes. D'abord, vu la conclusion que la courbe constituait un danger à cause de sa nature cachée et imprévue, ce n'est pas en se basant sur le témoignage de ceux qui empruntent quotidiennement le chemin qu'il est possible, à notre avis, de déterminer si cette courbe présentait un danger pour l'automobiliste moyen, ou si la municipalité aurait dû connaître l'existence du danger. De plus, en concluant que la municipalité

it is open for a trial judge to prefer some parts of the evidence over others, and to re-assess the trial judge's weighing of the evidence, is, with respect, not within the province of an appellate court.

63 As well, since the question of knowledge is to be approached from the perspective of a prudent municipal councillor, we find the evidence of lay witnesses to be of little assistance. In *Ryan*, *supra*, at para. 28, Major J. stated that the applicable standard of care is that which "would be expected of an ordinary, reasonable and prudent person in the same circumstances" (emphasis added). Municipal councillors are elected for the purpose of managing the affairs of the municipality. This requires some degree of study and of information gathering, above that of the average citizen of the municipality. Indeed, it may in fact require consultation with experts to properly meet the obligation to be informed. Although municipal councillors are not experts, to equate the "prudent municipal councillor" with the opinion of lay witnesses who live on the road is incorrect in our opinion.

64 It is in this context that we view the following comments of the trial judge, at para. 90:

> If the R.M. did not have actual knowledge of the danger inherent in this portion of Snake Hill Road, it should have known. While four accidents in 12 years may not in itself be significant, it takes on more significance given the close proximity of three of these accidents, the relatively low volume of traffic, the fact that there are permanent residences on the road and the fact that the road is frequented by young and perhaps less experienced drivers. I am not satisfied that the R.M. has established that in these circumstances it took reasonable steps to prevent this state of disrepair on Snake Hill Road from continuing.

aurait dû connaître le mauvais état du chemin, la juge de première instance a clairement choisi de ne pas se fonder sur les témoignages susmentionnés. Comme nous l'avons dit précédemment, le juge de première instance peut préférer certaines parties de la preuve à d'autres, et, en toute déférence, il n'appartient pas au tribunal d'appel de procéder à nouveau à l'appréciation de la preuve, tâche déjà accomplie par le juge du procès.

Qui plus est, étant donné que la question de la connaissance doit être considérée du point de vue du conseiller municipal prudent, nous estimons que le témoignage des témoins ordinaires est peu utile. Dans l'arrêt *Ryan*, précité, par. 28, le juge Major a dit que la norme de diligence qui s'applique est celle de la personne agissant aussi diligemment que « le ferait une personne ordinaire, raisonnable et prudente placée dans la même situation » (nous soulignons). Les conseillers municipaux sont élus pour gérer les affaires de la municipalité. Pour s'acquitter de cette tâche, il leur faut, dans un cas donné, examiner la situation et recueillir de l'information, faire davantage que ce que fait le simple citoyen de la municipalité. De fait, ils peuvent avoir à consulter des experts pour respecter leur obligation d'être informés. Bien que les conseillers municipaux ne soient pas des experts, il est à notre avis erroné d'assimiler le point de vue du « conseiller municipal prudent » à l'opinion de témoins ordinaires qui habitent sur le chemin.

C'est à la lumière de ce contexte que nous interprétons les commentaires suivants de la juge de première instance (au par. 90) :

> [TRADUCTION] Si la M.R. ne connaissait pas concrètement le danger intrinsèque que comporte cette portion du chemin Snake Hill, elle aurait dû le connaître. Le fait que quatre accidents se soient produits en 12 ans n'est peut-être pas significatif en soi, mais il le devient si l'on considère que trois de ces accidents sont survenus à proximité, qu'il s'agit d'une route à débit de circulation relativement faible, que des résidences permanentes sont situées en bordure de celle-ci et que le chemin est fréquenté par des conducteurs jeunes et peut-être moins expérimentés. Je ne suis pas convaincue que la M.R. a établi avoir, dans ces circonstances, pris des mesures raisonnables pour remédier au mauvais état du chemin Snake Hill.

From this statement, we take the trial judge to have meant that, given the occurrence of prior accidents on this low-traffic road, the existence of permanent residents, and the type of drivers on the road, the municipality did not take the reasonable steps it should have taken in order to ensure that Snake Hill Road did not contain a hazard such as the one in question. Based on these factors, the trial judge drew the inference that the municipality should have been put on notice and investigated Snake Hill Road, in which case it would have become aware of the hazard in question. This factual inference, grounded as it was on the trial judge's assessment of the evidence, was in our view, far from reaching the requisite standard of palpable and overriding error, proper.

Selon notre interprétation, la juge de première instance a voulu dire que, compte tenu des accidents antérieurs sur ce chemin à faible débit de circulation, de la présence de résidents permanents et du type de conducteurs qui empruntent le chemin, la municipalité n'a pas pris les mesures raisonnables qu'elle aurait dû prendre pour faire en sorte que le chemin Snake Hill ne comporte pas de danger comme celui en cause. À partir de ces éléments, la juge de première instance a inféré que la municipalité aurait dû être informée de la situation sur le chemin Snake Hill et aurait dû faire enquête à cet égard, ce qui lui aurait permis de prendre connaissance de l'existence du danger. Cette inférence factuelle, qui repose sur l'appréciation de la preuve faite par la juge de première instance, était selon nous fondée et loin de constituer l'erreur manifeste et dominante requise par la norme pertinente.

Although we agree with our colleague that the circumstances of the prior accidents in this case do not provide a direct basis for the municipality to have had knowledge of the particular hazard in question, in the view of the trial judge, they should have caused the municipality to investigate Snake Hill Road, which in turn would have resulted in actual knowledge. In this case, far from causing the municipality to investigate, the evidence of Mr. Danger, who had been the municipal administrator for 20 years, was that, until the time of the trial, he was not even aware of the three accidents which had occurred between 1978 and 1987 on Snake Hill Road. As such, we do not find that the trial judge based her conclusion on any perspective other than that of a prudent municipal councillor, and therefore that she did not commit an error of law in this respect. Moreover, we do not find that she imputed knowledge to the municipality on the basis of the occurrence of prior accidents on Snake Hill Road. The existence of the prior accidents was simply a factor which caused the trial judge to find that the municipality should have been put on notice with respect to the condition of Snake Hill Road (para. 90).

65 À l'instar de notre collègue, nous estimons que les circonstances des accidents survenus antérieurement, en l'espèce, ne constituent pas une preuve directe que la municipalité aurait dû avoir connaissance du danger particulier en cause, mais, selon la juge de première instance, ces circonstances auraient dû inciter la municipalité à faire enquête à l'égard du chemin Snake Hill, ce qui lui aurait permis de prendre connaissance concrètement du danger. Dans la présente affaire, les accidents antérieurs sont loin d'avoir incité la municipalité à faire enquête. D'ailleurs, M. Danger, administrateur de la municipalité pendant 20 ans, a témoigné que, jusqu'au procès, il n'était même pas au fait des trois accidents survenus entre 1978 et 1987 sur le chemin Snake Hill. En conséquence, nous n'estimons pas que la juge de première instance a fondé sa conclusion sur quelque autre point de vue autre que celui du conseiller municipal prudent, et elle n'a donc pas commis d'erreur de droit à cet égard. De plus, nous sommes d'avis qu'elle n'a pas prêté à la municipalité la connaissance requise sur la base des accidents antérieurs. L'existence de ces accidents ne constituait rien de plus qu'un des éléments qui l'ont amenée à conclure que la municipalité aurait dû être au fait de l'état du chemin Snake Hill (par. 90).

We emphasize that, in our view, the trial judge did not shift the burden of proof to the municipality

66 Nous tenons à souligner que la juge de première instance n'a pas, à notre avis, transféré le fardeau de

on this issue. Once the trial judge found that there was a permanent feature of Snake Hill Road which presented a hazard to the ordinary motorist, it was open to her to draw an inference that the municipality ought to have been aware of the danger. Once such an inference is drawn, then, unless the municipality can rebut the inference by showing that it took reasonable steps to prevent such a hazard from continuing, the inference will be left undisturbed. In our view, this is what the trial judge did in the above passage when she states: "I am not satisfied that the R.M. has established that in these circumstances it took reasonable steps to prevent this state of disrepair on Snake Hill Road from continuing" (para. 90 (emphasis added)). The fact that she drew such an inference is clear from the fact that this statement appears directly after her finding that the municipality ought to have known of the hazard based on the listed factors. Thus, it is our view that the trial judge did not improperly shift the burden of proof onto the municipality in this case.

la preuve à la municipalité sur cette question. Dès lors qu'elle a conclu qu'il existait sur le chemin Snake Hill une caractéristique permanente présentant un danger pour l'automobiliste moyen, il lui était loisible d'inférer que la municipalité aurait dû être au fait du danger. Dès l'instant où une telle inférence est tirée, elle demeure inchangée à moins que la municipalité ne puisse la réfuter en démontrant qu'elle a pris des mesures raisonnables pour faire cesser le danger. Selon nous, c'est ce que la juge de première instance a fait dans l'extrait précité lorsqu'elle dit : [TRADUCTION] « Je ne suis pas convaincue que la M.R. a établi avoir, dans ces circonstances, pris des mesures raisonnables pour remédier au mauvais état du chemin Snake Hill » (par. 90 (nous soulignons)). L'existence de cette inférence ressort clairement du fait que le passage précité suit immédiatement la conclusion de la juge de première instance selon laquelle, pour les raisons qu'elle énumère, la municipalité aurait dû connaître l'existence du danger. Par conséquent, nous sommes d'avis que la juge de première instance n'a pas fait erreur et transféré le fardeau de la preuve à la municipalité en l'espèce.

67 As well, although the circumstances of the prior accidents in this case do not provide strong evidence that the municipality ought to have known of the hazard, proof of prior accidents is not a necessary condition to a finding of breach of the duty of care under s. 192 of *The Rural Municipality Act, 1989*. If this were so, the first victim of an accident on a negligently maintained road would not be able to recover, whereas subsequent victims in identical circumstances would. Although under s. 192(3) the municipality cannot be held responsible for disrepair of which it could not have known, it is not sufficient for the municipality to wait for an accident to occur before remedying the disrepair, and, in the absence of proof by the plaintiff of prior accidents, claim that it could not have known of the hazard. If this were the case, not only would the first victim of an accident suffer a disproportionate evidentiary burden, but municipalities would also be encouraged not to collect information pertaining to accidents on its roads, as this would make it more difficult for the plaintiff in a motor vehicle accident to prove that the

De même, bien que les accidents survenus antérieurement en l'espèce ne constituent pas une preuve solide que la municipalité aurait dû connaître l'existence du danger, la preuve d'accidents antérieurs n'est pas une condition nécessaire pour qu'un tribunal puisse conclure à la violation de l'obligation de diligence prévue par l'art. 192 de la *Rural Municipality Act, 1989*. Si c'était le cas, la première victime d'un accident sur une route négligemment entretenue ne pourrait obtenir réparation, alors que les victimes subséquentes d'accidents survenant dans des circonstances identiques le pourraient. Bien que, au regard du par. 192(3), la municipalité ne puisse être tenue responsable du mauvais état d'une route dont elle n'aurait pu avoir connaissance, elle ne saurait se contenter d'attendre qu'un accident se produise avant de remédier au mauvais état de la route et, si un demandeur n'apporte pas la preuve de l'existence d'accidents antérieurs, soutenir qu'elle n'aurait pu connaître l'existence du danger. Dans cette hypothèse, non seulement imposerait-on à la première victime d'un accident un fardeau de preuve disproportionné, mais on encouragerait aussi

municipality knew or ought to have known of the disrepair.

Although in this case the trial judge emphasized the prior accidents that the plaintiff did manage to prove, in our view, it is not necessary to rely on these accidents in order to satisfy s. 192(3). For the plaintiff to provide substantial and concrete proof of the municipality's knowledge of the state of disrepair of its roads, is to set an impossibly high burden on the plaintiff. Such information was within the particular sphere of knowledge of the municipality, and in our view, it was reasonable for the trial judge to draw an inference of knowledge from her finding that there was an ongoing state of disrepair.

To summarize our position on this issue, we do not find that the trial judge erred in law either by failing to approach the question from the perspective of a prudent municipal councillor, or by improperly shifting the burden of proof onto the defendant. As such, it would require a palpable and overriding error in order to overturn her finding that the municipality knew or ought to have known of the hazard, and, in our view, no such error was made.

V. Causation

We agree with our colleague's statement at para. 159 that the trial judge's conclusions on the cause of the accident was a finding of fact: *Cork v. Kirby MacLean, Ltd.*, [1952] 2 All E.R. 402 (C.A.), at p. 407, quoted with approval in *Matthews v. MacLaren* (1969), 4 D.L.R. (3d) 557 (Ont. H.C.), at p. 566. Thus, this finding should not be interfered with absent palpable and overriding error.

les municipalités à ne pas recueillir d'informations concernant les accidents survenant sur leurs routes, puisqu'il serait en conséquence plus difficile à la victime d'un accident d'automobile qui intente des poursuites de prouver que la municipalité visée connaissait le mauvais état de la route ou aurait dû le connaître.

68 Bien que, en l'espèce, la juge de première instance ait souligné les accidents antérieurs dont le demandeur a effectivement prouvé l'existence, nous sommes d'avis qu'il n'est pas nécessaire de s'appuyer sur ces accidents pour satisfaire aux exigences du par. 192(3). Exiger du demandeur qu'il fournisse une preuve substantielle et tangible de la connaissance par la municipalité du mauvais état de ses routes revient à lui imposer un fardeau inacceptablement lourd. Il s'agit d'information relevant du domaine de connaissance de la municipalité et, selon nous, il était raisonnable que la juge de première instance infère de sa conclusion relative au mauvais état d'entretien persistant du chemin que la municipalité possédait la connaissance requise.

69 Pour résumer notre position sur cette question, nous ne pouvons conclure que la juge de première instance a commis une erreur de droit soit parce qu'elle aurait omis d'examiner la question du point de vue du conseiller municipal prudent, soit parce qu'elle aurait à tort transféré le fardeau de la preuve à la défenderesse. Par conséquent, il faudrait une erreur manifeste et dominante pour écarter sa conclusion que la municipalité connaissait le danger ou aurait dû le connaître et, selon nous, aucune erreur de cette nature n'a été commise.

V. Lien de causalité

70 Nous faisons nôtres les propos énoncés par notre collègue, au par. 159, selon lesquels la conclusion de la juge de première instance quant à la cause de l'accident était une conclusion de fait : *Cork c. Kirby MacLean, Ltd.*, [1952] 2 All E.R. 402 (C.A.), p. 407; cité et approuvé dans *Matthews c. MacLaren* (1969), 4 D.L.R. (3d) 557 (H.C. Ont.), p. 566. En conséquence, cette conclusion ne doit pas être modifiée en l'absence d'erreur manifeste et dominante.

71 The trial judge based her findings on causation on three points (at para. 101):

> (1) the accident occurred at a dangerous part of the road where a sign warning motorists of the hidden hazard should have been erected;
>
> (2) even if there had been a sign, Mr. Nikolaisen's degree of impairment did increase his risk of not reacting, or reacting inappropriately, to a sign;
>
> (3) even so, Mr. Nikolaisen was not driving recklessly such that one would have expected him to have missed or ignored a warning sign. Moments before, on departing the Thiel residence, he had successfully negotiated a sharp curve which he could see and which was apparent to him.

The trial judge concluded that, on a balance of probabilities, Mr. Nikolaisen would have reacted and possibly avoided an accident, if he had been given advance warning of the curve. However she also found that the accident was partially caused by the conduct of Mr. Nikolaisen, and apportioned fault accordingly, with 50 percent to Mr. Nikolaisen and 35 percent to the Rural Municipality (para. 102).

72 As noted above, this Court has previously held that "an omission is only a material error if it gives rise to the reasoned belief that the trial judge must have forgotten, ignored or misconceived the evidence in a way that affected his conclusion" (*Van de Perre*, *supra*, at para.15). In the present case, it is not clear from the trial judge's reasons which portions of the evidence of Mr. Laughlin, Craig and Toby Thiel and Paul Housen she relied upon, or to what extent. However, as we have already stated, the full evidentiary record was before the trial judge and, absent further proof that the omission in her reasons was due to her misapprehension or neglect, of the evidence, we can presume that she reviewed the evidence in its entirety and based her factual findings

La juge de première instance a fondé ses conclusions au sujet du lien de causalité sur trois éléments (au par. 101) :

> (1) l'accident est survenu à un endroit dangereux du chemin, où un panneau de signalisation aurait dû être installé pour avertir les automobilistes du danger caché;
>
> (2) même s'il y avait eu un panneau de signalisation, le degré d'ébriété de M. Nikolaisen avait accru chez lui le risque qu'il ne réagisse pas du tout ou de façon inappropriée à une signalisation;
>
> (3) malgré cela, M. Nikolaisen ne conduisait pas de façon si téméraire qu'il était à prévoir qu'il ne voit pas un panneau de signalisation ou n'en tienne pas compte. Quelques instants plus tôt, à son départ de la résidence des Thiel, il avait pris avec succès un virage serré qu'il pouvait clairement voir.

La juge de première instance a estimé que, selon la prépondérance des probabilités, M. Nikolaisen aurait réagi et peut-être évité l'accident si on lui avait signalé à l'avance la présence de la courbe. Toutefois, elle a également conclu que l'accident avait été causé en partie par la conduite de M. Nikolaisen, et elle a réparti la responsabilité en conséquence, soit dans une proportion de 50 p. 100 à M. Nikolaisen et de 35 p. 100 à la municipalité rurale (par. 102).

Comme nous l'avons indiqué précédemment, notre Cour a jugé, dans une autre affaire, qu'« une omission ne constitue une erreur importante que si elle donne lieu à la conviction rationnelle que le juge de première instance doit avoir oublié, négligé d'examiner ou mal interprété la preuve de telle manière que sa conclusion en a été affectée » (*Van de Perre*, précité, par. 15). En l'espèce, les motifs de la juge de première instance n'indiquent pas clairement sur quelles parties des témoignages de M. Laughlin, de Craig et Toby Thiel et de Paul Housen elle s'est appuyée, ni dans quelle mesure elle l'a fait. Cependant, comme nous l'avons dit plus tôt, la juge de première instance disposait de l'ensemble de la preuve et, en l'absence d'autre élément

on this review. This presumption, absent sufficient evidence of misapprehension or neglect, is consistent with the high level of error required by the test of "palpable and overriding" error. We reiterate that it is open to the trial judge to prefer the testimony of certain witnesses over others and to place more weight on some parts of the evidence than others, particularly where there is conflicting evidence: *Toneguzzo-Norvell*, *supra*, at pp. 122-23. The mere fact that the trial judge did not discuss a certain point or certain evidence in depth is not sufficient grounds for appellate interference: *Van de Perre*, *supra*, at para. 15.

indiquant que cette omission dans ses motifs résulte du fait qu'elle aurait mal interprété des éléments de la preuve ou négligé d'en examiner certains, nous pouvons présumer qu'elle a examiné l'ensemble de la preuve et que ses conclusions de fait reposaient sur cet examen. En l'absence de preuve établissant de façon suffisante qu'il y a eu mauvaise interprétation d'éléments de preuve ou négligence d'examiner certains de ceux-ci, cette présomption permet de conclure à l'absence d'erreur importante du type de celle requise pour satisfaire au critère de l'erreur « manifeste et dominante ». Nous tenons à rappeler que le juge de première instance peut préférer le témoignage de certains témoins et accorder plus de poids à certaines parties de la preuve qu'à d'autres, particulièrement en présence de preuves contradictoires : *Toneguzzo-Norvell*, précité, p. 122-123. Le simple fait que la juge de première instance n'a pas analysé en profondeur un point donné ou un élément de preuve particulier ne constitue pas un motif suffisant pour justifier l'intervention des tribunaux d'appel : *Van de Perre*, précité, par. 15.

For these reasons, we do not feel it appropriate to review the evidence of Mr. Laughlin and the lay witnesses *de novo*. As we concluded earlier, the trial judge's finding of fact that a hidden hazard existed at the curve should not be interfered with. The finding of a hidden hazard that requires a sign formed part of the basis of her findings concerning causation. As her conclusions on the existence of a hidden hazard had a basis in the evidence, her conclusions on causation grounded in part on the hidden hazard finding also had a basis in the evidence.

73 Pour ces motifs, nous n'estimons pas opportun d'examiner à nouveau les dépositions de M. Laughlin et des témoins ordinaires. Comme nous l'avons affirmé précédemment, il n'y a pas lieu de modifier la conclusion de fait de la juge de première instance selon laquelle la courbe présentait un danger caché. Ses conclusions touchant le lien de causalité reposent en partie sur cette conclusion relative à l'existence d'un danger caché nécessitant l'installation d'un panneau d'avertissement. Tout comme ses conclusions relatives à l'existence d'un danger caché, celles touchant le lien de causalité — fondées en partie sur le danger caché — avaient elles aussi des assises dans la preuve.

As for the silence of the trial judge on the evidence of Mr. Laughlin, we observe only that the evidence of Mr. Laughlin appears to be general in nature and thus of limited utility. Mr. Laughlin admitted that he could only provide general comments on the effects of alcohol on motorists, but could not provide specific expertise on the actual effect of alcohol on an individual driver. This is significant, as the level of tolerance of an individual driver plays a key role in determining the actual effect of alcohol on the

74 Pour ce qui est du silence de la juge de première instance concernant le témoignage de M. Laughlin, signalons simplement que ce témoignage paraît être de nature générale et, partant, d'une utilité limitée. M. Laughlin a reconnu qu'il ne pouvait faire que des observations générales quant aux effets de l'alcool sur les automobilistes, et non apporter une expertise particulière sur l'effet concret de l'alcool sur un conducteur donné. Il s'agit d'un point important, puisque le seuil de tolérance d'un conducteur donné

motorist; an experienced drinker, although dangerous, will probably perform better on the road than an inexperienced drinker. It is noteworthy that the trial judge believed the evidence of Mr. Anderson that Mr. Nikolaisen's vehicle was travelling at the relatively slow speed of between 53 to 65 km/h at the time of impact with the embankment. It was also permissible for the trial judge to rely on the evidence of lay witnesses that Mr. Nikolaisen had successfully negotiated an apparently sharp curve moments before the accident, rather than relying on the evidence of Mr. Laughlin, which was of a hypothetical and unspecific nature. Indeed, the hypothetical nature of Mr. Laughlin's evidence reflects the entire inquiry into whether Mr. Nikolaisen would have seen a sign and reacted, or the precise speed that would be taken by a reasonable driver upon approaching the curve. The abstract nature of such inquiries supports deference to the factual findings of the trial judge, and is consistent with the stringent standard imposed by the phrase "palpable and overriding error".

75 Therefore we conclude that the trial judge's factual findings on causation were reasonable and thus do not reach the level of a palpable and overriding error, and therefore should not have been interfered with by the Court of Appeal.

VI. Common Law Duty of Care

76 As we conclude that the municipality is liable under *The Rural Municipality Act, 1989*, we find it unnecessary to consider the existence of a common law duty in this case.

VII. Disposition

77 As we stated at the outset, there are important reasons and principles for appellate courts not to interfere improperly with trial decisions. Applying

joue un rôle essentiel dans la détermination de l'effet concret de l'alcool sur cet automobiliste; bien que dangereuse, la personne qui a l'habitude de boire se débrouillera probablement mieux sur la route qu'une personne qui n'en a pas l'habitude. Il convient de souligner que la juge de première instance a cru le témoignage de M. Anderson selon lequel le véhicule de M. Nikolaisen roulait à une vitesse relativement faible, soit entre 53 et 65 km/h, au moment de l'impact avec le remblai. Il lui était également permis de retenir les dépositions des témoins ordinaires selon lesquelles M. Nikolaisen avait réussi à prendre un virage apparemment serré quelques instants avant l'accident, plutôt que le témoignage de M. Laughlin, lequel était de nature hypothétique et générale. De fait, la nature hypothétique du témoignage de M. Laughlin est représentative de toute l'analyse de la question de savoir si M. Nikolaisen aurait aperçu un panneau de signalisation et aurait réagi en conséquence, ou à quelle vitesse précise un conducteur raisonnable s'approcherait du virage. Le caractère théorique de ces analyses justifie de faire montre de retenue à l'égard des conclusions factuelles de la juge de première instance et permet d'affirmer qu'on n'a pas satisfait à la norme rigoureuse imposée par l'expression « erreur manifeste et dominante ».

Par conséquent, nous estimons que les constatations factuelles de la juge de première instance concernant la causalité étaient raisonnables, qu'elles ne constituent donc pas une erreur manifeste et dominante et, partant, que la Cour d'appel n'aurait pas dû les modifier.

VI. Obligation de diligence prévue par la common law

Puisque nous concluons à la responsabilité de la municipalité en vertu de la *Rural Municipality Act, 1989*, nous n'estimons pas nécessaire de nous demander s'il existe en l'espèce une obligation de diligence prévue par la common law.

VII. Dispositif

Comme nous l'avons dit au départ, d'importantes raisons et d'importants principes commandent aux tribunaux d'appel de ne pas modifier indûment

these reasons and principles to this case, we would allow the appeal, set aside the judgment of the Saskatchewan Court of Appeal, and restore the judgment of the trial judge, with costs throughout.

The reasons of Gonthier, Bastarache, Binnie and LeBel JJ. were delivered by

BASTARACHE J. (dissenting) —

I. Introduction

This appeal arises out of a single-vehicle accident which occurred on July 18, 1992, on Snake Hill Road, a rural road located in the Municipality of Shellbrook, Saskatchewan. The appellant, Paul Housen, a passenger in the vehicle, was rendered a quadriplegic by the accident. At trial, the judge found that the driver of the vehicle, Douglas Nikolaisen, was negligent in travelling Snake Hill Road at an excessive rate of speed and in operating his vehicle while impaired. The trial judge also found the respondent, the Municipality of Shellbrook, to be at fault for breaching its duty to keep the road in a reasonable state of repair as required by s. 192 of *The Rural Municipality Act, 1989*, S.S. 1989-90, c. R-26.1. The Court of Appeal overturned the trial judge's finding that the respondent municipality was negligent. At issue in this appeal is whether the Court of Appeal had sufficient grounds to intervene in the decision of the lower court. The respondent has also asked this Court to overturn the trial judge's finding that the respondent knew or ought to have known of the alleged disrepair of Snake Hill Road and that the accident was caused in part by the negligence of the respondent. An incidental question is whether a common law duty of care exists alongside the statutory duty imposed on the respondent by s. 192.

les décisions des tribunaux de première instance. Appliquant ces raisons et principes à la présente espèce, nous sommes d'avis d'accueillir le pourvoi, d'infirmer le jugement de la Cour d'appel de la Saskatchewan et de rétablir la décision de la juge de première instance, avec dépens devant toutes les cours.

Version française des motifs des juges Gonthier, Bastarache, Binnie et LeBel rendus par

LE JUGE BASTARACHE (dissident) —

I. Introduction

Le présent pourvoi découle d'un accident impliquant un seul véhicule survenu le 18 juillet 1992 sur le chemin Snake Hill, route rurale située dans la municipalité de Shellbrook, en Saskatchewan. L'appelant, Paul Housen, qui était passager dans le véhicule, est devenu quadriplégique à la suite de cet accident. Au procès, la juge a conclu que le conducteur du véhicule, Douglas Nikolaisen, avait fait preuve de négligence en roulant à une vitesse excessive sur le chemin Snake Hill et en conduisant son véhicule pendant que ses facultés étaient affaiblies. La juge de première instance a également estimé que l'intimée, la municipalité de Shellbrook, avait commis une faute en manquant à l'obligation de tenir le chemin dans un état raisonnable d'entretien comme le lui impose l'art. 192 de la loi intitulée la *Rural Municipality Act, 1989*, S.S. 1989-90, ch. R-26.1. La Cour d'appel a infirmé la décision de la juge de première instance concluant à la négligence de la municipalité intimée. La question en litige dans le présent pourvoi consiste à déterminer si la Cour d'appel avait des motifs suffisants pour modifier la décision du tribunal de première instance. L'intimée demande également à notre Cour d'infirmer les conclusions de la juge de première instance portant que l'intimée connaissait ou aurait dû connaître le mauvais état dans lequel se trouvait, prétend-on, le chemin Snake Hill, et que l'accident a été causé en partie par sa négligence. Il faut également répondre à la question incidente de savoir si une obligation de diligence de common law coexiste avec l'obligation légale imposée à l'intimée par l'art. 192.

79 I conclude that the Court of Appeal was correct to overturn the trial judge's finding that the respondent was negligent. Though I would not interfere with the trial judge's factual findings on this issue, I find that she erred in law by failing to apply the correct standard of care. I would also overturn the trial judge's conclusions with regard to knowledge and causation. In coming to the conclusion that the respondent knew or should have known of the alleged disrepair of Snake Hill Road, the trial judge erred in law by failing to consider the knowledge requirement from the perspective of a prudent municipal councillor and by failing to be attentive to the fact that the onus of proof was on the appellant. In addition, the trial judge drew an unreasonable inference by imputing knowledge to the respondent on the basis of accidents that occurred on other segments of the road while motorists were travelling in the opposite direction. The trial judge also erred with respect to causation. She misapprehended the evidence before her, drew erroneous conclusions from that evidence and ignored relevant evidence. Finally, I would not interfere with the decision of the courts below to reject the appellant's argument that a common law duty existed. It is unnecessary to impose a common law duty of care where a statutory duty exists. Moreover, the application of common law negligence principles would not affect the outcome in these proceedings.

J'estime que la Cour d'appel a eu raison d'infirmer la conclusion de la juge de première instance selon laquelle la municipalité intimée a été négligente. Je ne modifierais pas les conclusions de fait de la juge de première instance sur cette question, mais je suis d'avis qu'elle a commis une erreur de droit en n'appliquant pas la norme de diligence appropriée. J'infirmerais également ses conclusions en ce qui concerne la question de la connaissance et le lien de causalité. En concluant que l'intimée connaissait ou aurait dû connaître le mauvais état dans lequel se trouvait, prétend-on, le chemin Snake Hill, la juge de première instance a commis une erreur de droit en n'appréciant pas l'exigence relative à la connaissance du point de vue du conseiller municipal prudent et en ne tenant pas compte du fait que le fardeau de la preuve incombait à l'appelant. De plus, la juge de première instance a tiré une inférence déraisonnable en prêtant à l'intimée la connaissance requise, en raison d'accidents survenus sur d'autres tronçons du chemin alors que des automobilistes circulaient en sens inverse. La juge de première instance a également commis une erreur relativement au lien de causalité. Elle a mal interprété la preuve qui lui était soumise, elle en a tiré des conclusions erronées et elle n'a pas tenu compte d'éléments de preuve pertinents. Enfin, je ne modifierais pas la décision des juridictions inférieures ayant rejeté l'argument de l'appelant selon lequel il existait une obligation de diligence de common law. Il est inutile d'imposer une obligation de common law lorsqu'il existe une obligation légale. Qui plus est, l'application des principes de la common law en matière de négligence n'aurait aucune incidence sur l'issue de la présente instance.

II. Factual Background

80 The sequence of` events which culminated in this tragic accident began to unfold some 19 hours before its occurrence on the afternoon of July 18, 1992. On July 17, Mr. Nikolaisen attended a barbeque at the residence of Craig and Toby Thiel, located on Snake Hill Road. He arrived in the late afternoon and had his first drink of the day at approximately 6:00 p.m. He consumed four or five drinks before leaving the Thiel residence at approximately

II. Les faits

La suite d'événements ayant abouti au tragique accident a commencé quelque 19 heures avant l'accident lui-même, dans l'après-midi du 18 juillet 1992. Le 17 juillet, M. Nikolaisen a participé à un barbecue à la résidence de Craig et Toby Thiel, sur le chemin Snake Hill. Arrivé en fin d'après-midi, il a pris son premier verre de la journée vers 18 h. Il en a pris quatre ou cinq avant de quitter la résidence des Thiel vers 22 h ou 22 h 30. Après avoir passé

10:00 or 10:30 p.m. After returning home for a few hours, Mr. Nikolaisen proceeded to the Sturgeon Lake Jamboree, where he met up with the appellant. At the jamboree, Mr. Nikolaisen consumed eight or nine double rye drinks and several beers. The appellant was also drinking during this event. The appellant and Mr. Nikolaisen partied on the grounds of the jamboree for several hours. At approximately 4:30 a.m., the appellant left the jamboree with Mr. Nikolaisen. After travelling around the back roads for a period of time, they returned to the Thiel residence. It was approximately 8:00 a.m. The appellant and Mr. Nikolaisen had several more drinks over the course of the morning. Mr. Nikolaisen stopped drinking two or three hours before leaving the Thiel residence with the appellant at approximately 2:00 p.m.

A light rain was falling when the appellant and Mr. Nikolaisen left the Thiel residence, travelling eastbound with Mr. Nikolaisen behind the wheel of a Ford pickup truck. The truck swerved or "fish-tailed" as it turned the corner from the Thiel driveway onto Snake Hill Road. As Mr. Nikolaisen continued on his way over the course of a gentle bend some 300 metres in length, gaining speed to an estimated 65 km/h, the truck again fish-tailed several times. The truck went into a skid as Mr. Nikolaisen approached and entered a sharper right turn. Mr. Nikolaisen steered into the skid but was unable to negotiate the curve. The left rear wheel of the truck contacted an embankment on the left side of the road. The vehicle travelled on the road for approximately 30 metres when the left front wheel contacted and climbed an 18-inch embankment on the left side of the road. This second contact with the embankment caused the truck to enter a 360-degree roll with the passenger side of the roof contacting the ground first.

When the vehicle came to rest, the appellant was unable to feel any sensation. Mr. Nikolaisen climbed out the back window of the vehicle and ran to the Thiel residence for assistance. Police later accompanied Mr. Nikolaisen to the Shellbrook Hospital where a blood sample was taken. Expert testimony estimated Mr. Nikolaisen's blood alcohol level to be

quelques heures chez lui, M. Nikolaisen s'est rendu au jamboree de Sturgeon Lake, où il a rencontré l'appelant. Sur les lieux du jamboree, M. Nikolaisen a consommé huit ou neuf ryes doubles et plusieurs bières. L'appelant buvait lui aussi. L'appelant et M. Nikolaisen ont fait la fête sur les lieux du jamboree pendant plusieurs heures. Vers 4 h 30, l'appelant a quitté le jamboree en compagnie de M. Nikolaisen. Après avoir roulé sur des routes de campagne pendant un certain temps, ils sont retournés à la résidence des Thiel. Il était environ 8 h. L'appelant et M. Nikolaisen ont pris plusieurs autres verres au cours de la matinée. M. Nikolaisen a cessé de boire deux ou trois heures avant de quitter la résidence des Thiel en compagnie de l'appelant vers 14 h.

81 Une faible pluie tombait lorsque l'appelant et M. Nikolaisen ont quitté la résidence des Thiel et pris la route, en direction est, à bord d'une camionnette Ford conduite par M. Nikolaisen. L'arrière de la camionnette a zigzagué lorsque le véhicule a tourné à l'intersection de l'entrée de la résidence des Thiel et du chemin Snake Hill. Alors que M. Nikolaisen prenait un léger virage d'une longueur de quelque 300 mètres, tout en accélérant à 65 km/h environ, l'arrière de sa camionnette a zigzagué à nouveau à plusieurs reprises. La camionnette s'est mise à déraper lorsque M. Nikolaisen a amorcé un virage plus serré vers la droite. Il a donné un coup de volant, mais n'a pas réussi à prendre le virage. La roue arrière gauche de la camionnette a heurté un remblai situé du côté gauche du chemin. Le véhicule a continué sa course sur une distance d'environ 30 mètres, puis sa roue avant gauche est montée sur un remblai de 18 pouces du côté gauche du chemin, après l'avoir heurté. Sous la force du second impact, la camionnette a fait un tonneau complet, le toit du côté du passager touchant le sol en premier.

82 Lorsque le véhicule s'est immobilisé, l'appelant n'éprouvait plus aucune sensation. M. Nikolaisen s'est hissé hors du véhicule par la fenêtre arrière et a couru chez les Thiel pour demander de l'aide. Plus tard, la police a accompagné M. Nikolaisen à l'hôpital de Shellbrook, où un échantillon de sang a été prélevé. Le témoignage d'expert a révélé

between 180 and 210 milligrams in 100 millilitres of blood at the time of the accident, well over the legal limits prescribed in *The Highway Traffic Act*, S.S. 1986, c. H-3.1, and the *Criminal Code*, R.S.C. 1985, c. C-46.

83 Mr. Nikolaisen had travelled on Snake Hill Road three times in the 24 hours preceding the accident, but had not driven it on any earlier occasions. The road was about a mile and three quarters in length and was flanked by highways to the north and to the east. Starting at the north end, it ran south for a short distance, dipped between open fields, then curved to the southeast and descended in a southerly loop down and around Snake Hill, past trees, bush and pasture, to the bottom of the valley. There it curved sharply to the southeast as it passed the Thiels' driveway. Once it passed the driveway, it curved gently to the south east for about 300 metres, then curved more distinctly to the south. It was on this stretch that the accident occurred. From that point on, the road crossed a creek, took another curve, then ascended a steep hill to the east, straightened out, and continued east for just over half a mile, past tree-lined fields and another farm site, to an approach to the highway.

84 Snake Hill Road was established in 1923 and was maintained by the respondent municipality for the primary purpose of providing local farmers access to their fields and pastures. It also served as an access road for the two permanent residences and one veterinary clinic located on it. The road at its northernmost end, coming off the highway, is characterized as a "Type C" local access road under the provincial government's scheme of road classification. This means that it is graded, gravelled and elevated above the surrounding land. The portion of the road east of the Thiel residence, on which the accident occurred, is characterized as "Type B" bladed trail, essentially a prairie trail that has been bladed to remove the ruts and to allow it to be driven on. Bladed trails follow the path of least resistance through the surrounding land and are not elevated or gravelled. The

que, au moment de l'accident, l'alcoolémie de M. Nikolaisen se situait entre 180 et 210 milligrammes par 100 milligrammes, taux largement supérieur à la limite permise par la loi intitulée la *Highway Traffic Act*, S.S. 1986 ch. H-3.1, et par le *Code criminel*, L.R.C. 1985, ch. C-46.

M. Nikolaisen avait emprunté le chemin Snake Hill à trois reprises au cours des 24 heures ayant précédé l'accident, mais il n'y avait jamais circulé auparavant. Ce chemin, flanqué de routes au nord et à l'est, fait environ un mille et trois quarts de longueur. À partir de son extrémité nord, il franchit une courte distance en direction sud, traverse des champs, puis tourne vers le sud-est pour ensuite descendre en lacet vers le sud autour du mont Snake Hill, passant devant des arbres, buissons et pâturages, jusqu'au fond de la vallée. De là, il tourne brusquement vers le sud-est devant l'entrée de la résidence des Thiel. Tout de suite après, il tourne doucement vers le sud-est sur une distance d'environ 300 mètres, puis décrit une courbe plus prononcée vers le sud. C'est à cet endroit que l'accident s'est produit. De là, le chemin traverse un ruisseau, tourne encore, puis monte une pente raide vers l'est, se redresse et continue vers l'est sur une distance d'un peu plus d'un demi mille et passe devant des champs bordés d'arbres et une autre ferme, jusqu'à une voie d'accès à la route.

Construit en 1923, le chemin Snake Hill est entretenu par la municipalité intimée dans le but premier de permettre aux fermiers de la région d'accéder à leurs champs et pâturages. Il sert également de voie d'accès à deux résidences permanentes et à une clinique vétérinaire. Le tronçon nord du chemin, dont l'extrémité part de la route, est considéré comme un chemin d'accès local de « type C » selon le système provincial de classification des routes. Cela signifie qu'il est nivelé, gravelé et possède une chaussée surélevée. Le tronçon du chemin situé à l'est de la résidence des Thiel et sur lequel l'accident s'est produit est considéré comme un chemin nivelé de « type B », c'est-à-dire essentiellement un chemin dont les ornières ont été remplies pour le rendre carrossable. Les chemins nivelés suivent le tracé qui présente le moins d'obstacle à travers le terrain environnant et ne sont ni surélevés ni gravelés. La

province of Saskatchewan has some 45,000 kilometres of bladed trails.

According to the provincial scheme of road classification, both bladed trails and local access roads are "non-designated", meaning that they are not subject to the Saskatchewan Rural Development Sign Policy and Standards. On such roads, the council of the rural municipality makes a decision to post signs if it becomes aware of a hazard or if there are several accidents at one specific spot. Three accidents had occurred on Snake Hill Road between 1978 and 1987. All three accidents occurred to the east of the site of the Nikolaisen rollover, with drivers travelling westbound. A fourth accident occurred on Snake Hill Road in 1990 but there was no evidence as to where it occurred. There was no evidence that topography was a factor in any of these accidents. The respondent municipality had not posted signs on any portion of Snake Hill Road.

III. Relevant Statutory Provisions

The Rural Municipality Act, 1989, S.S. 1989-90, c. R-26.1

192(1) Every Council shall keep in a reasonable state of repair all municipal roads, dams and reservoirs and the approaches to them that have been constructed or provided by the municipality or by any person with the permission of the council or that have been constructed or provided by the province, having regard to the character of the municipal road, dam or reservoir and the locality in which it is situated or through which it passes.

. . .

(2) Where the council fails to carry out its duty imposed by subsections (1) and (1.1), the municipality is, subject to *The Contributory Negligence Act*, civilly liable for all damages sustained by any person by reason of the failure.

province de Saskatchewan compte quelque 45 000 kilomètres de chemins nivelés.

85 Selon le système de classification des routes, tant les chemins nivelés que les chemins d'accès local sont [TRADUCTION] « non désignés », c'est-à-dire qu'ils ne sont pas visés par le document intitulé *Saskatchewan Rural Development Sign Policy and Standards* (« Politique et normes de signalisation routière en milieu rural en Saskatchewan »). Le conseil de la municipalité rurale installe des panneaux de signalisation sur ces chemins s'il constate l'existence d'un danger ou si plusieurs accidents se produisent au même endroit. Trois accidents sont survenus sur le chemin Snake Hill de 1978 à 1987. Tous ces accidents se sont produits à l'est de l'endroit où la camionnette de Nikolaisen a fait un tonneau et les véhicules concernés circulaient en direction ouest. Un quatrième accident s'est produit sur le chemin Snake Hill en 1990, mais aucune preuve indiquant l'endroit exact de l'accident n'a été présentée. Rien ne permettait de conclure que la topographie des lieux était à l'origine de l'un ou l'autre de ces accidents. La municipalité intimée n'avait installé aucun panneau signalisateur le long du chemin Snake Hill.

III. Les dispositions législatives pertinentes

86 *The Rural Municipality Act, 1989*, S.S. 1989-90, ch. R-26.1

[TRADUCTION]

192(1) Le conseil tient dans un état raisonnable d'entretien tous les chemins municipaux, barrages et réservoirs, ainsi que les accès à ces ouvrages qui ont été construits ou sont fournis par la municipalité ou par toute autre personne avec la permission du conseil ou qui ont été construits ou sont fournis par le gouvernement de la province, eu égard à la nature de l'ouvrage en question et à la localité où il est situé ou qu'il traverse.

. . .

(2) Lorsque le conseil omet de s'acquitter des obligations qui lui incombent en vertu des paragraphes (1) et (1.1), la municipalité est, sous réserve de la *Contributory Negligence Act* [*Loi sur le partage de la responsabilité*], civilement responsable des dommages subis par toute personne à la suite de ce manquement.

(3) Default under subsections (1) and (1.1) shall not be imputed to a municipality in any action without proof by the plaintiff that the municipality knew or should have known of the disrepair of the municipal road or other thing mentioned in subsections (1) and (1.1).

The Highway Traffic Act, S.S. 1986, c. H-3.1

33(1) Subject to the other provisions of this Act, no person shall drive a vehicle on a highway:

(a) at a speed greater than 80 kilometres per hour; or

(b) at a speed greater than the maximum speed indicated by any signs that are erected on the highway . . . .

(2) No person shall drive a vehicle on a highway at a speed greater than is reasonable and safe in the circumstances.

44(1) No person shall drive a vehicle on a highway without due care and attention.

(3) En cas d'action reprochant un manquement visé aux paragraphes (1) et (1.1) la responsabilité de la municipalité concernée n'est engagée que si le demandeur établit que cette dernière connaissait ou aurait dû connaître le mauvais état du chemin municipal ou autre ouvrage mentionné aux paragraphes (1) et (1.1).

The Highway Traffic Act, S.S. 1986, ch. H-3.1

[TRADUCTION]

33(1) Sous réserve des autres dispositions de la présente loi, il est interdit de conduire sur une voie publique à une vitesse supérieure, selon le cas :

a) à 80 kilomètres à l'heure;

b) à la vitesse maximale indiquée par la signalisation routière le long de la voie publique en question . . .

(2) Il est interdit de conduire un véhicule sur une voie publique à une vitesse supérieure à celle qui est raisonnable et sécuritaire dans les circonstances.

44(1) Il est interdit de conduire un véhicule sur une voie publique sans faire preuve de la prudence et de l'attention nécessaires.

IV. Judicial History

A. *Saskatchewan Court of Queen's Bench*, [1998] 5 W.W.R. 523

87 Wright J. found the respondent negligent in failing to erect a sign to warn motorists of the sharp right curve on Snake Hill Road, which she characterized as a "hidden hazard". She also found Mr. Nikolaisen negligent in travelling Snake Hill Road at an excessive speed and in operating his vehicle while impaired. The appellant was held to be contributorily negligent in accepting a ride with Mr. Nikolaisen. Fifteen percent of the fault was apportioned to the appellant, and the remainder was apportioned jointly and severally 50 percent to Mr. Nikolaisen and 35 percent to the respondent.

88 Wright J. found that s. 192 of *The Rural Municipality Act, 1989* imposed a statutory duty of care on the respondent toward persons travelling on Snake Hill Road. She then considered whether the respondent met the standard of care as delineated in

IV. L'historique des procédures judiciaires

A. *Cour du Banc de la Reine de la Saskatchewan*, [1998] 5 W.W.R. 523

La juge Wright a conclu que l'intimée avait fait preuve de négligence en omettant d'installer un panneau signalant aux automobilistes l'existence du virage à droite serré sur le chemin Snake Hill, virage qu'elle a qualifié de [TRADUCTION] « danger caché ». Elle a également estimé que M. Nikolaisen avait été négligent en roulant à une vitesse excessive sur le chemin Snake Hill et en conduisant son véhicule pendant qu'il avait les facultés affaiblies. L'appelant a été tenu responsable de négligence concourante parce qu'il avait accepté de monter à bord du véhicule de M. Nikolaisen. La responsabilité a été partagée ainsi : 15 p. 100 à l'appelant, le reste étant réparti solidairement entre M. Nikolaisen (50 p. 100) et l'intimée (35 p. 100).

La juge Wright a d'abord conclu que l'art. 192 de la *Rural Municipality Act, 1989* imposait à l'intimée une obligation légale de diligence envers les personnes circulant sur le chemin Snake Hill. Elle s'est ensuite demandée si l'intimée s'était

s. 192 and the jurisprudence interpreting that section. She referred specifically to *Partridge v. Rural Municipality of Langenberg*, [1929] 3 W.W.R. 555 (Sask. C.A.), in which it was stated at p. 558 that "the road must be kept in such a reasonable state of repair that those requiring to use it may, exercising ordinary care, travel upon it with safety". She also cited *Shupe v. Rural Municipality of Pleasantdale*, [1932] 1 W.W.R. 627 (Sask. C.A.), at p. 630: "[R]egard must be had to the locality . . . the situation of the road therein, whether required to be used by many or by few; . . . to the number of roads to be kept in repair; to the means at the disposal of the council for that purpose, and the requirements of the public who use the road." Relying on *Galbiati v. City of Regina*, [1972] 2 W.W.R. 40 (Sask. Q.B.), Wright J. observed that although the Act does not mention an obligation to erect warning signs, the general duty of repair nevertheless includes the duty to warn motorists of a hidden hazard.

conformée à la norme de diligence énoncée à l'art. 192 et dans la jurisprudence portant sur l'interprétation de cet article. Elle a fait état, en particulier, de l'arrêt *Partridge c. Rural Municipality of Langenberg*, [1929] 3 W.W.R. 555, dans lequel la Cour d'appel de la Saskatchewan a déclaré, à la p. 558, que [TRADUCTION] « le chemin doit être tenu dans un état raisonnable d'entretien, de façon que ceux qui doivent l'emprunter puissent, en prenant des précautions normales, y circuler en sécurité ». Elle a également cité le passage suivant de l'affaire *Shupe c. Rural Municipality of Pleasantdale*, [1932] 1 W.W.R. 627 (C.A. Sask.), p. 630 : [TRADUCTION] « [I]l faut tenir compte de la localité où est situé le chemin, [. . .] de son emplacement dans celle-ci, se demander s'il sera beaucoup ou peu fréquenté; [. . .] du nombre de chemins à entretenir; des ressources budgétaires dont dispose le conseil à cette fin et des besoins du public qui emprunte ce chemin ». Se fondant sur l'affaire *Galbiati c. City of Regina*, [1972] 2 W.W.R. 40 (B.R. Sask.), la juge Wright a fait observer que, bien que la Loi ne mentionne pas explicitement l'obligation d'installer des panneaux d'avertissement, l'obligation générale d'entretien comporte néanmoins celle de signaler aux automobilistes l'existence d'un danger caché.

Having laid out the relevant case law, Wright J. went on to discuss the character of the road. Relying primarily on the evidence of two experts at trial, Mr. Anderson and Mr. Werner, she found that the sharp right turning curve was a hazard that was not readily apparent to the users of the road. From their testimony she concluded (at para. 85):

89

Après avoir fait état de la jurisprudence pertinente, la juge Wright a poursuivi en examinant la nature du chemin. S'appuyant principalement sur les témoignages donnés par deux experts au procès, MM. Anderson et Werner, elle a conclu que le virage à droite serré constituait un danger que les usagers du chemin ne pouvaient voir aisément. De leurs témoignages, elle a tiré la conclusion suivante (au par. 85) :

It is a hidden hazard. The location of the Nikolaisen rollover is the most dangerous segment of Snake Hill Road. Approaching the location of the Nikolaisen rollover, limited sight distance, created by uncleared bush, precludes a motorist from being forewarned of an impending sharp right turn immediately followed by a left turn. While there were differing opinions on the *maximum* speed at which this curve can be negotiated, I am satisfied that when limited sight distance is combined with the tight radius of the curve and lack of superelevation, this curve cannot be *safely* negotiated at speeds greater

[TRADUCTION] Il s'agit d'un danger caché. L'endroit où le véhicule de M. Nikolaisen a fait un tonneau est situé sur le tronçon le plus dangereux du chemin Snake Hill. À l'approche de cet endroit, des broussailles réduisent la distance de visibilité de l'automobiliste et l'empêchent de voir l'imminence d'un virage à droite serré, qui est immédiatement suivi d'un virage à gauche. Bien que des opinions divergentes aient été émises quant à la vitesse *maximale* à laquelle ce virage peut être pris, je suis d'avis que, vu la distance de visibilité réduite, l'existence d'une courbe serrée et l'absence de surélévation du chemin, ce

than 60 kilometres per hour when conditions are favourable, or 50 kilometres per hour when wet. [Emphasis in original.]

virage ne peut être pris en sécurité à une vitesse supérieure à 60 kilomètres à l'heure dans des conditions favorables, ou 50 kilomètres à l'heure sur chaussée humide. [En italique dans l'original.]

Wright J. then noted that, while it would not be reasonable to expect the respondent to construct the road to a higher standard or to clear all of the bush away, it was reasonable to expect the respondent to erect and maintain a warning or regulatory sign "so that a motorist, using ordinary care, may be forewarned, adjust speed and take corrective action in advance of entering a dangerous situation" (para. 86).

La juge Wright a ensuite précisé que, bien qu'on ne puisse raisonnablement exiger de l'intimée qu'elle construise le chemin selon une norme plus élevée ou qu'elle enlève toutes les broussailles, il était raisonnable de s'attendre à ce qu'elle installe et maintienne un panneau d'avertissement ou de signalisation [TRADUCTION] « afin qu'un automobiliste prenant des précautions normales soit prévenu et puisse réduire sa vitesse et prendre des mesures correctives avant d'arriver à l'endroit dangereux » (par. 86).

90 Wright J. then considered s. 192(3) of the Act, which provides that there is no breach of the statutory standard of care unless the municipality knew or should have known of the danger. Wright J. observed that between 1978 and 1990, there were four accidents on Snake Hill Road, three of which occurred "in the same vicinity" as the Nikolaisen rollover, and two of which were reported to the authorities. On the basis of this information, she held that "[i]f the R.M. [Rural Municipality] did not have actual knowledge of the danger inherent in this portion of Snake Hill Road, it should have known" (para. 90). Wright J. also found significant the relatively low volume of traffic on the road, the fact that there were permanent residences on the road, and the fact that the road was frequented by young and perhaps less experienced drivers.

La juge Wright a ensuite analysé le par. 192(3) de la Loi, qui prévoit qu'il n'y a manquement à l'obligation de diligence que si la municipalité connaissait ou aurait dû connaître l'existence du danger. Elle a rappelé que quatre accidents étaient survenus sur le chemin Snake Hill de 1978 à 1990. Trois de ceux-ci se sont produits [TRADUCTION] « aux environs » de l'endroit où le véhicule de M. Nikolaisen a fait un tonneau, et deux ont été signalés aux autorités. Sur la base de cette information, elle a conclu que [TRADUCTION] « [s]i la M.R. [municipalité rurale] ne connaissait pas concrètement le danger intrinsèque que comporte cette portion du chemin Snake Hill, elle aurait dû le connaître » (par. 90). La juge Wright a également accordé de l'importance au débit relativement faible de la circulation sur le chemin, au fait que des résidences permanentes étaient situées en bordure de celui-ci et au fait que le chemin était fréquenté par des conducteurs jeunes et peut-être moins expérimentés.

91 In respect to causation, Wright J. found that it was probable that a warning sign would have enabled Mr. Nikolaisen to take corrective action to maintain control of his vehicle despite the fact of his impairment. She concluded (at para. 101):

En ce qui concerne le lien de causalité, la juge Wright a estimé qu'un panneau de signalisation aurait probablement permis à M. Nikolaisen de prendre des mesures correctives et de conserver la maîtrise de son véhicule, même si ses facultés étaient affaiblies. Elle a aussi tiré la conclusion suivante, au par. 101 :

Mr. Nikolaisen's degree of impairment only served to increase the risk of him not reacting, or reacting inappropriately to a sign. Mr. Nikolaisen was not driving recklessly such that he would have intentionally disregarded

[TRADUCTION] Le degré d'ébriété de M. Nikolaisen n'a fait qu'accroître le risque qu'il ne réagisse pas du tout ou encore de façon inappropriée à une signalisation. M. Nikolaisen ne conduisait pas de façon si téméraire qu'il

a warning or regulatory sign. He had moments earlier, when departing the Thiel residence, successfully negotiated a sharp curve which he could see and which was apparent to him.

Wright J. also addressed the appellant's argument that the municipality was in breach of a common law duty of care which was not qualified or limited by any of the restrictions set out under s. 192. She held that *Just v. British Columbia*, [1989] 2 S.C.R. 1228, and the line of authority both preceding and following that decision did not apply to the case before her given the existence of the statutory duty of care. She also found that any qualifying words in s. 192 of the Act pertained to the standard of care and did not impose limitations on the statutory duty of care.

B. *Saskatchewan Court of Appeal*, [2000] 4 W.W.R. 173, 2000 SKCA 12

On appeal, Cameron J.A., writing for a unanimous court, dealt primarily with the trial judge's finding that the respondent's failure to place a warning sign or regulatory sign at the site of the accident constituted a breach of its statutory duty of road repair. He did not find it necessary to rule on the issue of causation given his conclusion that the trial judge erred in finding the respondent negligent.

Cameron J.A. characterized the trial judge's conclusion that the respondent had breached the statutory duty of care as a matter of mixed fact and law. He noted that an appellate court is not to interfere with a trial judge's findings of fact unless the judge made a "palpable and overriding error" which affected his or her assessment of the facts. With respect to errors of law, however, Cameron J.A. remarked that the ability of an appellate court to overturn the finding of the trial judge is "largely unbounded". Regarding errors of mixed fact and law, Cameron J.A. noted that these are typically subject to the same standard of review as findings

aurait intentionnellement fait abstraction d'un panneau d'avertissement ou de signalisation. Quelques instants plus tôt, au moment de quitter la résidence des Thiel, il avait pris avec succès un virage serré qu'il pouvait clairement voir.

92 La juge Wright s'est également penchée sur l'argument de l'appelant voulant que la municipalité ait manqué à une obligation de diligence de common law qui ne serait pas atténuée ou restreinte par l'une ou l'autre des dispositions de l'art. 192. Elle a estimé que l'arrêt *Just c. Colombie-Britannique*, [1989] 2 R.C.S. 1228, ainsi que la jurisprudence antérieure et postérieure à cette décision ne s'appliquaient pas à l'affaire dont elle était saisie, vu l'existence de l'obligation légale de diligence. Elle a également jugé que les termes restrictifs de l'art. 192 de la Loi visaient la norme de diligence et n'avaient pas pour effet de limiter la portée de l'obligation légale de diligence.

B. *Cour d'appel de la Saskatchewan*, [2000] 4 W.W.R. 173, 2000 SKCA 12

93 En appel, exprimant la décision unanime de la cour, le juge Cameron s'est attaché principalement à la conclusion de la juge de première instance portant que, en omettant d'installer un panneau d'avertissement ou de signalisation à l'endroit de l'accident, l'intimée avait manqué à son obligation légale d'entretien des routes. Il n'a pas jugé nécessaire de se prononcer sur la question du lien de causalité, vu sa conclusion que la juge de première instance avait commis une erreur en déclarant l'intimée responsable de négligence.

94 Le juge Cameron a qualifié la conclusion de la juge de première instance que l'intimée avait manqué à son obligation légale de diligence de conclusion portant sur une question mixte de fait et de droit. Il a souligné qu'une cour d'appel ne doit pas modifier les conclusions de fait du juge de première instance à moins que ce dernier n'ait commis une « erreur manifeste et dominante » ayant faussé son appréciation des faits. Pour ce qui est des erreurs de droit, toutefois, le juge Cameron a fait remarquer que le pouvoir d'une cour d'appel d'infirmer la conclusion du juge de première instance est [TRADUCTION] « presque illimité ». En ce qui concerne les erreurs

of fact. One exception to this, according to Cameron J.A., occurs where the trial judge identifies the correct legal test, yet fails to apply one branch of that test to the facts at hand. As support for this proposition, Cameron J.A. cited (at para. 41) Iacobucci J. in *Canada (Director of Investigation and Research) v. Southam Inc.*, [1997] 1 S.C.R. 748, at para. 39:

> [I]f a decision-maker says that the correct test requires him or her to consider A, B, C, and D, but in fact the decision-maker considers only A, B, and C, then the outcome is as if he or she had applied a law that required consideration of only A, B, and C. If the correct test requires him or her to consider D as well, then the decision-maker has in effect applied the wrong law, and so has made an error of law.

95 Turning to the applicable law in this case, Cameron J.A. acknowledged that the standard of care set out in the Act and the jurisprudence interpreting it requires municipalities to post warning signs to warn of hazards that prudent drivers, using ordinary care, would be unlikely to appreciate. Based on the jurisprudence, Cameron J.A. set out (at para. 50) an analytical framework to be used in order to assess if a municipality has breached its duty in this regard. This framework requires the judge:

> 1. To determine the character and state of the road at the time of the accident. This, of course, is a matter of fact that entails an assessment of the material features of the road where the accident occurred, as well as those factors going to the maintenance standard, namely the location, class of road, patterns of use, and so on.
>
> 2. To assess the issue of whether persons requiring to use the road, exercising ordinary car[e], could ordinarily travel upon it safely. This is essentially a reasonable person test, one concerned with how a

mixtes de fait et de droit, le juge Cameron a précisé qu'elles sont normalement assujetties à la même norme de contrôle que les conclusions de fait. Selon le juge Cameron, cette règle générale souffre une exception, qui s'applique dans les cas où, bien que le juge du procès ait retenu le bon critère juridique applicable, il omet d'en appliquer un élément aux faits de l'affaire dont il est saisi. Au soutien de cette affirmation, le juge Cameron a cité, au par. 41, les propos suivants du juge Iacobucci dans l'arrêt *Canada (Directeur des enquêtes et recherches) c. Southam Inc.*, [1997] 1 R.C.S. 748, par. 39 :

> [Si] un décideur dit que, en vertu du critère applicable, il lui faut tenir compte de A, B, C et D, mais que, dans les faits, il ne prend en considération que A, B et C, alors le résultat est le même que s'il avait appliqué une règle de droit lui dictant de ne tenir compte que de A, B et C. Si le bon critère lui commandait de tenir compte aussi de D, il a en fait appliqué la mauvaise règle de droit et commis, de ce fait, une erreur de droit.

Relativement au droit applicable en l'espèce, le juge Cameron a reconnu que la norme de diligence énoncée dans la Loi et dans la jurisprudence portant sur l'interprétation de cette loi exige des municipalités qu'elles installent des panneaux de mise en garde pour signaler les dangers que les conducteurs prudents et prenant des précautions normales ne pourraient vraisemblablement pas mesurer. Se fondant sur la jurisprudence, le juge Cameron a établi, au par. 50, un cadre analytique permettant de déterminer si une municipalité a manqué à son obligation à cet égard. Suivant ce cadre, le juge doit examiner les aspects suivants :

[TRADUCTION]

> 1. Le juge doit déterminer la nature et l'état du chemin au moment de l'accident. Il s'agit, bien sûr, d'une question de fait, qui nécessite une appréciation des caractéristiques physiques du chemin à l'endroit où l'accident s'est produit, ainsi que de tous les facteurs se rapportant à la norme d'entretien, à savoir l'emplacement du chemin, le type de chemin dont il s'agit, les utilisations habituelles de celui-ci, et ainsi de suite.
>
> 2. Il soit se demander si les personnes qui devaient emprunter le chemin pouvaient généralement, en prenant des précautions normales, y circuler en sécurité. Il s'agit essentiellement du critère de la

reasonable driver on that particular road would have conducted himself or herself. It is necessary in taking this step to take account of the various elements noted in the authorities referred to earlier, namely the locality of the road, the character and class of the road, the standard to which the municipality could reasonably have been expected to maintain the road, and so forth. These criteria fall to be balanced in the context of the question: how would a reasonable driver have driven upon this particular road? Since this entails the application of a legal standard to a given set of facts, it constitutes a question of mixed fact and law.

3. To determine either tha[t] the road was in a reasonable state of repair or that it was not, depending upon the assessment made while using the second step. If it is determined that the road was not in a reasonable state of repair, then it becomes necessary to go on to determine whether the municipality knew or should have known of the state of disrepair before imputing liability.

According to Cameron J.A., the trial judge did not err in law by failing to set out the proper legal test. She did, however, make an error in law of the type identified by Iacobucci J. in *Southam*, *supra.* In his view, when applying the law to the facts of the case, the trial judge failed to assess the manner in which a reasonable driver, exercising ordinary care, would ordinarily have driven on the road, and the risk, if any, that the unmarked curve might have posed for the ordinary driver. As noted by Cameron J.A., the trial judge "twice alluded to the matter, but failed to come to grips with it" (para. 57).

Cameron J.A. also found that the trial judge had made a "palpable and overriding" error of fact in determining that the respondent had breached the standard of care. According to Cameron J.A., the trial judge's factual error stemmed from her reliance on the expert testimony of Mr. Werner and Mr. Anderson. Cameron J.A. found that the evidence of both experts was based on the fundamental premise

personne raisonnable, qui sert à déterminer comment se serait comporté un conducteur raisonnable sur ce chemin en particulier. À cette étape, il faut tenir compte des nombreux facteurs énoncés dans la jurisprudence mentionnée précédemment, c'est-à-dire l'emplacement du chemin, la nature et le type du chemin, la norme d'entretien à laquelle on pouvait raisonnablement s'attendre d'une municipalité, et ainsi de suite. Ces facteurs doivent être soupesés dans le contexte de la question suivante : Comment un conducteur raisonnable aurait-il conduit son véhicule sur ce chemin en particulier? Puisque cette question suppose l'application d'une norme juridique à un ensemble donné de faits, elle constitue une question mixte de fait et de droit.

3. Il doit déterminer si le chemin était dans un état raisonnable d'entretien, compte tenu des conclusions tirées à la deuxième étape. S'il est établi que le chemin ne se trouvait pas dans un état raisonnable d'entretien, il faut alors déterminer si la municipalité connaissait ou aurait dû connaître le mauvais état d'entretien avant de conclure à la responsabilité de celle-ci.

96 Selon le juge Cameron, la juge de première instance n'a pas commis d'erreur de droit en ce qui concerne le critère juridique applicable. Elle a cependant commis une erreur de droit du genre de celle exposée par le juge Iacobucci dans l'arrêt *Southam*, précité. À son avis, lorsqu'elle a appliqué le droit aux faits de l'espèce, la juge de première instance a omis, d'une part, de se demander comment un conducteur raisonnable, faisant montre de prudence normale, aurait conduit son véhicule sur ce chemin, et, d'autre part, d'évaluer le risque, s'il en est, que le virage non annoncé aurait pu constituer pour le conducteur moyen. Comme l'a souligné le juge Cameron de la Cour d'appel, la juge de première instance [TRADUCTION] « a évoqué la question à deux reprises, mais elle ne l'a pas abordée » (par. 57).

97 Le juge Cameron a également estimé que la juge de première instance avait commis une erreur de fait « manifeste et dominante » en concluant que l'intimée n'avait pas exercé le degré de diligence requis. Selon le juge Cameron, cette erreur de fait découlait de l'importance accordée par la juge Wright aux témoignages d'experts de MM. Werner et Anderson. À son avis, les témoignages de ces deux experts

that the ordinary driver could be expected to travel the road at a speed of 80 km/h. In his view, this premise was misconceived and unsupported by the evidence.

98 Cameron J.A. concluded that although the trial judge was free to accept the evidence of some witnesses over others, she was not free to accept expert testimony that was based on an erroneous factual premise. According to Cameron J.A., had the trial judge found that a prudent driver, exercising ordinary care for his or her safety, would not ordinarily have driven this section of Snake Hill Road at a speed greater than 60 km/h, then she would have had to conclude that no hidden hazard existed since the curve could be negotiated safely at this speed.

99 Cameron J.A. agreed with the trial judge that a common law duty of care was not applicable in this case. His remarks in this respect are found at para. 44 of his reasons:

> Concerning the duty of care, it might be noted that unlike statutory provisions empowering municipalities to maintain roads, but imposing no duty upon them to do so, the duty in this instance owes its existence to a statute, rather than the neighbourhood principle of the common law: *Just v. British Columbia*, [1989] 2 S.C.R. 1228 (S.C.C.). The duty is readily seen to extend to all who travel upon the roads.

V. Issues

100 A. Did the Court of Appeal properly interfere with the trial judge's finding that the respondent was in breach of its statutory duty of care?

B. Did the trial judge err in finding the respondent knew or should have known of the alleged danger?

C. Did the trial judge err in finding that the accident was caused in part by the respondent's negligence?

reposaient sur la prémisse fondamentale qu'on pouvait s'attendre à ce que le conducteur moyen circule sur le chemin à une vitesse de 80 km/h. Selon lui, cette prémisse était erronée et n'était pas étayée par la preuve.

Le juge Cameron a conclu que, bien qu'il fût loisible à la juge de première instance d'accorder davantage foi à certains témoignages qu'à d'autres, il ne lui était pas loisible de retenir un témoignage d'expert fondé sur une prémisse factuelle erronée. Selon lui, si la juge de première instance avait estimé qu'un conducteur prudent prenant des précautions normales pour assurer sa sécurité n'aurait généralement pas roulé sur cette portion du chemin Snake Hill à plus de 60 km/h, alors elle aurait dû conclure à l'absence de danger caché puisque le virage pouvait être pris en sécurité à cette vitesse.

Le juge Cameron a souscrit à l'opinion de la juge de première instance que l'obligation de diligence de common law ne s'appliquait pas en l'espèce. Il a fait les commentaires suivants à ce sujet, au par. 44 de ses motifs :

> [TRADUCTION] En ce qui concerne l'obligation de diligence, il convient de préciser que, contrairement aux dispositions législatives qui habilitent les municipalités à entretenir les chemins, sans toutefois leur imposer l'obligation de le faire, en l'espèce l'obligation doit son existence à une loi, plutôt qu'au principe de common law fondé sur la proximité : *Just c. Colombie-Britannique*, [1989] 2 R.C.S. 1228. On saisit immédiatement que l'obligation de diligence existe en faveur de tous ceux qui circulent sur les routes.

V. Les questions en litige

A. La Cour d'appel a-t-elle eu raison de modifier la conclusion de la juge de première instance portant que l'intimée avait manqué à son obligation légale de diligence?

B. La juge de première instance a-t-elle commis une erreur en concluant que l'intimée connaissait ou aurait dû connaître le danger allégué?

C. La juge de première instance a-t-elle commis une erreur en concluant que l'accident a été en partie causé par la négligence de l'intimée?

D. Does a common law duty of care coexist alongside the statutory duty of care?

VI. Analysis

A. *Did the Court of Appeal Properly Interfere with the Decision at Trial?*

(1) The Standard of Review

Although the distinctions are not always clear, the issues that confront a trial court fall generally into three categories: questions of law, questions of fact, and questions of mixed law and fact. Put briefly, questions of law are questions about what the correct legal test is; questions of fact are questions about what actually took place between the parties; and questions of mixed law and fact are questions about whether the facts satisfy the legal tests (*Southam*, *supra*, at para. 35).

Of the three categories above, the highest degree of deference is accorded to the trial judge's findings of fact. The Court will not overturn a factual finding unless it is palpably and overridingly, or clearly wrong (*Southam*, *supra*, at para. 60; *Stein v. The Ship "Kathy K"*, [1976] 2 S.C.R. 802, at p. 808; *Toneguzzo-Norvell (Guardian ad litem of) v. Burnaby Hospital*, [1994] 1 S.C.R. 114, at p. 121). This deference is principally grounded in the recognition that only the trial judge enjoys the opportunity to observe witnesses and to hear testimony first-hand, and is therefore better able to choose between competing versions of events (*Schwartz v. Canada*, [1996] 1 S.C.R. 254, at para. 32). It is however important to recognize that the making of a factual finding often involves more than merely determining the who, what, where and when of the case. The trial judge is very often called upon to draw inferences from the facts that are put before the court. For example, in this case, the trial judge inferred from the fact of accidents having occurred on Snake Hill Road

D. Est-ce qu'une obligation de diligence de common law coexiste avec l'obligation légale de diligence?

VI. L'analyse

A. *La Cour d'appel a-t-elle eu raison de modifier la décision de la juge de première instance?*

(1) La norme de contrôle

101 Bien qu'elles ne soient pas toujours faciles à distinguer, les questions auxquelles doit répondre un tribunal de première instance se classent généralement en trois catégories : les questions de droit, les questions de fait et les questions mixtes de fait et de droit. En résumé, les questions de droit concernent la détermination du critère juridique applicable; les questions de fait portent sur ce qui s'est réellement passé entre les parties et les questions mixtes de fait et de droit consistent à déterminer si les faits satisfont au critère juridique (*Southam*, précité, par. 35).

102 De ces trois catégories, ce sont les conclusions de fait du juge de première instance qui commandent le degré le plus élevé de retenue. La Cour ne modifie les conclusions de fait du juge de première instance que si celui-ci a commis une erreur manifeste ou dominante ou si la conclusion est manifestement erronée (*Southam*, précité, par. 60; *Stein c. Le navire « Kathy K »*, [1976] 2 R.C.S. 802, p. 808; *Toneguzzo-Norvell (Tutrice à l'instance de) c. Burnaby Hospital*, [1994] 1 R.C.S. 114, p. 121). Cette retenue repose principalement sur le fait que, puisqu'il est le seul à avoir l'occasion d'observer les témoins et d'entendre les témoignages de vive voix, le juge de première instance est en conséquence plus à même de choisir entre deux versions divergentes d'un même événement (*Schwartz c. Canada*, [1996] 1 R.C.S. 254, par. 32). Cependant, il est important de reconnaître que tirer une conclusion de fait implique souvent davantage que le simple fait de déterminer qui a fait quoi, ainsi que où et quand il l'a fait. Le juge de première instance est très souvent appelé à faire des inférences à partir des faits qui lui sont

that the respondent knew or should have known of the hidden danger.

103 This Court has determined that a trial judge's inferences of fact should be accorded a similar degree of deference as findings of fact (*Geffen v. Goodman Estate*, [1991] 2 S.C.R. 353). In reviewing the making of an inference, the appeal court will verify whether it can reasonably be supported by the findings of fact that the trial judge reached and whether the judge proceeded on proper legal principles. I respectfully disagree with the majority's view that inferences can be rejected only where the inference-drawing process itself is deficient: see *Toronto (City) Board of Education v. O.S.S.T.F., District 15*, [1997] 1 S.C.R. 487, at para. 45:

> When a court is reviewing a tribunal's findings of fact or the inferences made on the basis of the evidence, it can only intervene "where the evidence, viewed reasonably, is incapable of supporting a tribunal's findings of fact": *Lester (W. W.) (1978) Ltd. v. United Association of Journeymen and Apprentices of the Plumbing and Pipefitting Industry, Local 740*, [1990] 3 S.C.R. 644, at p. 669 *per* McLachlin J.

An inference can be clearly wrong where the factual basis upon which it relies is deficient or where the legal standard to which the facts are applied is misconstrued. My colleagues recognize themselves that a judge is often called upon to make inferences of mixed law and fact (para. 26). While the standard of review is identical for both findings of fact and inferences of fact, it is nonetheless important to draw an analytical distinction between the two. If the reviewing court were to review only for errors of fact, then the decision of the trial judge would necessarily be upheld in every case where evidence existed to support his or her factual findings. In my view, this Court is entitled to conclude that inferences made by the trial judge were clearly wrong, just as it is entitled to reach this conclusion in respect to findings of fact.

présentés. En l'espèce, par exemple, la juge de première instance a inféré du fait que des accidents s'étaient produits sur le chemin Snake Hill que l'intimée connaissait ou aurait dû connaître l'existence du danger caché.

Notre Cour a jugé qu'il fallait appliquer aux inférences de fait du juge de première instance le même degré de retenue qu'à ses conclusions de fait (*Geffen c. Succession Goodman*, [1991] 2 R.C.S. 353). La cour d'appel qui contrôle la validité d'une inférence se demande si celle-ci peut raisonnablement être étayée par les conclusions de fait tirées par le juge de première instance et si celui-ci a appliqué les principes juridiques appropriés. En toute déférence, je ne partage pas l'opinion de la majorité selon laquelle des inférences ne peuvent être rejetées que dans les cas où le processus qui les a produites est lui-même déficient : voir *Conseil de l'éducation de Toronto (Cité) c. F.E.E.E.S.O., district 15*, [1997] 1 R.C.S. 487, par. 45 :

> Lorsqu'une cour de justice contrôle les conclusions de fait d'un tribunal administratif ou les inférences qu'il a tirées de la preuve, elle ne peut intervenir que « lorsque les éléments de preuve, perçus de façon raisonnable, ne peuvent étayer les conclusions de fait du tribunal » : *Lester (W.W.) (1978) Ltd. c. Association unie des compagnons et apprentis de l'industrie de la plomberie et de la tuyauterie, section locale 740*, [1990] 3 R.C.S. 644, à la p. 669, le juge McLachlin.

Une inférence peut être manifestement erronée si ses assises factuelles présentent des lacunes ou si la norme juridique appliquée aux faits est mal interprétée. Mes collègues eux-mêmes reconnaissent qu'un juge est souvent appelé à tirer des inférences mixtes de fait et droit (par. 26). Bien que la norme de contrôle soit la même et pour les conclusions de fait et pour les inférences de fait, il importe néanmoins de faire une distinction analytique entre les deux. Si le tribunal de révision ne faisait que vérifier s'il y a des erreurs de fait, la décision du juge de première instance serait alors nécessairement confirmée dans tous les cas où il existe des éléments de preuve étayant les conclusions de fait de ce dernier. Selon moi, notre Cour a le droit de conclure que les inférences du juge de première instance étaient manifestement erronées, tout comme elle peut le faire à l'égard des conclusions de fait.

My colleagues take issue with the above statement that an appellate court will verify whether the making of an inference can reasonably be supported by the trial judge's findings of fact, a standard which they believe to be less strict than the "palpable and overriding" standard. I do not agree that a less strict standard is implied. In my view there is no difference between concluding that it was "unreasonable" or "palpably wrong" for a trial judge to draw an inference from the facts as found by him or her and concluding that the inference was not reasonably supported by those facts. The distinction is merely semantic.

104 Mes collègues ne sont pas d'accord avec l'énoncé susmentionné — savoir celui portant que la cour d'appel se demande si une inférence peut raisonnablement être étayée par les conclusions de fait tirées par le juge de première instance — estimant qu'il s'agit d'une norme de contrôle moins exigeante que celle de l'erreur « manifeste et dominante ». Pour ma part, je ne crois pas que cet énoncé implique l'application d'une norme moins exigeante. À mon avis, il n'y a aucune différence entre le fait de conclure qu'il était « déraisonnable » ou « manifestement erroné » pour un juge de tirer une inférence des faits qu'il a constatés, et le fait de conclure que cette inférence n'était pas raisonnablement étayée par ces faits. La distinction est purement sémantique.

By contrast, an appellate court reviews a trial judge's findings on questions of law not merely to determine if they are reasonable, but rather to determine if they are correct; *Moge v. Moge*, [1992] 3 S.C.R. 813, at p. 833; *R. v. Nova Scotia Pharmaceutical Society*, [1992] 2 S.C.R. 606, at p. 647; R. P. Kerans, *Standards of Review Employed by Appellate Courts* (1994), at p. 90. The role of correcting errors of law is a primary function of the appellate court; therefore, that court can and should review the legal determinations of the lower courts for correctness.

105 En revanche, une cour d'appel ne contrôle pas les conclusions tirées par le juge de première instance à l'égard des questions de droit simplement pour déterminer si elles sont raisonnables, mais plutôt pour déterminer si elles sont correctes : *Moge c. Moge*, [1992] 3 R.C.S. 813, p. 833; *R. c. Nova Scotia Pharmaceutical Society*, [1992] 2 R.C.S. 606, p. 647; R. P. Kerans, *Standards of Review Employed by Appellate Courts* (1994), p. 90. Un des rôles principaux d'une cour d'appel consiste à corriger les erreurs de droit et, par conséquent, cette cour peut et doit vérifier si les conclusions juridiques de la juridiction inférieure sont correctes.

In the law of negligence, the question of whether the conduct of the defendant has met the appropriate standard of care is necessarily a question of mixed fact and law. Once the facts have been established, the determination of whether or not the standard of care was met by the defendant will in most cases be reviewable on a standard of correctness since the trial judge must appreciate the facts within the context of the appropriate standard of care. In many cases, viewing the facts through the legal lens of the standard of care gives rise to a policy-making or law-setting function that is the purview of both the trial and appellate courts. As stated by Kerans, *supra*, at p. 103, "[t]he evaluation of facts as meeting or not meeting a legal test is a process that involves law-making. Moreover, it is probably correct to say that *every* new attempt to apply a legal rule to a set of

106 Dans le contexte du droit relatif à la négligence, la question de savoir si la conduite du défendeur est conforme à la norme de diligence appropriée est forcément une question mixte de fait et de droit. Une fois les faits établis, la décision touchant la question de savoir si le défendeur a respecté ou non la norme de diligence est, dans la plupart des cas, contrôlable selon la norme de la décision correcte, puisque le juge de première instance doit apprécier les faits au regard de la norme de diligence appropriée. Dans bien des cas, l'examen des faits à travers le prisme juridique de la norme de diligence implique l'établissement de politiques d'intérêt général ou la création de règles de droit, rôle qui relève autant des cours de première instance que des cours d'appel. Comme l'a dit Kerans, *op. cit.*, p. 103, [TRADUCTION] « [l]'examen de la

facts involves some measure of interpretation of that rule, and thus more law-making" (emphasis in original).

107 In a negligence case, the trial judge is called on to decide whether the conduct of the defendant was reasonable under all the circumstances. While this determination involves questions of fact, it also requires the trial judge to assess what is reasonable. As stated above, in many cases, this will involve a policy-making or "law-setting" role which an appellate court is better situated to undertake (Kerans, *supra*, at pp. 5-10). For example, in this case, the degree of knowledge that the trial judge should have imputed to the reasonably prudent municipal councillor raised the policy consideration of the type of accident-reporting system that a small rural municipality with limited resources should be expected to maintain. This law-setting role was recognized by the United States Supreme Court in *Bose Corp. v. Consumers Union of U.S., Inc.*, 466 U.S. 485 (1984), at note 17, within the context of an action for defamation:

> A finding of fact in some cases is inseparable from the principles through which it was deduced. At some point, the reasoning by which a fact is "found" crosses the line between application of those ordinary principles of logic and common experience which are ordinarily entrusted to the finder of fact into the realm of a legal rule upon which the reviewing court must exercise its own independent judgment. Where the line is drawn varies according to the nature of the substantive law at issue. Regarding certain largely factual questions in some areas of the law, the stakes — in terms of impact on future cases and future conduct — are too great to entrust them finally to the judgment of the trier of fact.

question de savoir si les faits satisfont ou non à un critère juridique donné est un processus qui implique une fonction créatrice de droit. Qui plus est, il est probablement exact d'affirmer que *chaque* nouvelle tentative d'appliquer une règle de droit à un ensemble de faits emporte une certaine interprétation de cette règle et, partant, l'élaboration de règles de droit additionnelles » (en italique dans l'original).

Dans une affaire de négligence, le juge de première instance est appelé à décider si la conduite du défendeur était raisonnable eu égard à toutes les circonstances. Bien que la prise de cette décision demande l'examen de questions de fait, elle exige également du juge de première instance qu'il établisse ce qui est raisonnable. Comme il a été mentionné plus tôt, dans bien des cas cette décision implique l'établissement de politiques d'intérêt général ou la « création de règles de droit », rôle qu'une cour d'appel est mieux placée pour remplir (Kerans, *op. cit.*, p. 5 à 10). En l'espèce, par exemple, le degré de connaissance que la juge de première instance aurait dû prêter au conseiller municipal raisonnablement prudent soulevait une considération participant d'une politique d'intérêt général, savoir le genre de système d'information sur les accidents qu'une petite municipalité rurale aux ressources budgétaires limitées est censée tenir. Ce rôle créateur de droit a été reconnu par la Cour suprême des États-Unis dans l'arrêt *Bose Corp. c. Consumers Union of U.S., Inc.*, 466 U.S. 485 (1984), à la note 17, dans le contexte d'une action en diffamation :

> [TRADUCTION] Une conclusion de fait est, dans certains cas, indissociable des principes qui ont été appliqués pour y arriver. À un point donné, le raisonnement menant à la « constatation d'un fait » cesse d'être l'application des principes ordinaires de logique et d'expérience générale, qui est généralement l'apanage du juge de première instance, pour devenir l'application d'une règle de droit, tâche où le tribunal de révision doit exercer son propre jugement. Cette ligne de démarcation se déplace selon la nature de la règle de droit substantiel en litige. Dans quelques branches du droit, certaines questions largement factuelles soulèvent des enjeux — incidence sur d'éventuelles affaires et le comportement futur — qui sont trop importants pour être confiés en premier et dernier ressort au juge de première instance.

My colleagues assert that the question of whether or not the standard of care was met by the defendant in a negligence case is subject to a standard of palpable and overriding error unless it is clear that the trial judge made some extricable error in principle with respect to the characterization of the standard or its application, in which case the error may amount to an error of law (para. 36). I disagree. In many cases, it will not be possible to "extricate" a purely legal question from the standard of care analysis applicable to negligence, which is a question of mixed fact and law. In addition, while some questions of mixed fact and law may not have "any great precedential value" (*Southam*, *supra*, at para. 37), such questions often necessitate a normative analysis that should be reviewable by an appellate court.

108 Mes collègues affirment que la question de savoir si, dans une affaire de négligence, le défendeur a respecté ou non la norme de diligence appropriée est assujettie au critère de l'erreur manifeste et dominante, sauf si le juge de première instance a clairement commis une erreur de principe isolable relativement à la détermination de la norme à appliquer ou à son application, auquel cas l'erreur peut constituer une erreur de droit (par. 36). Je ne suis pas d'accord. Dans bon nombre de cas, il ne sera pas possible d'« isoler » une question de droit pur de l'analyse de la norme de diligence applicable en matière de négligence, qui est une question mixte de fait et de droit. En outre, bien que certaines questions mixtes de fait et de droit puissent ne pas avoir « une grande valeur comme précédents » (*Southam*, précité, par. 37), ces questions impliquent souvent une analyse normative que devrait pouvoir contrôler une cour d'appel.

Consider again the issue of whether the municipality knew or should have known of the alleged danger. As a matter of law, the trial judge must approach the question of whether knowledge should be imputed to the municipality having regard to the duties of the ordinary, reasonable and prudent municipal councillor. If the trial judge applies a different legal standard, such as the reasonable person standard, it is an error of law. Yet even if the trial judge correctly identifies the applicable legal standard, he or she may still err in the process of assessing the facts through the lens of that legal standard. For example, there may exist evidence that an accident had previously occurred on the portion of the road on which the relevant accident occurred. In the course of considering whether or not that fact satisfies the legal test for knowledge the trial judge must make a number of normative assumptions. The trial judge must consider whether the fact that one accident had previously occurred in the same location would alert the ordinary, reasonable and prudent municipal councillor to the existence of a hazard. The trial judge must also consider whether the ordinary, reasonable and prudent councillor would have been alerted to the previous accident by an accident-reporting system. In my view, the question of whether the fact of a previous accident having occurred fulfills the applicable knowledge

109 Revenons maintenant à la question de savoir si la municipalité connaissait ou aurait dû connaître le danger allégué. Sur le plan juridique, le juge de première instance doit se demander s'il y a lieu de prêter cette connaissance à la municipalité eu égard aux obligations qui incombent au conseiller municipal moyen, raisonnable et prudent. Si le juge de première instance applique une autre norme juridique, par exemple celle de la personne raisonnable, il commet une erreur de droit. Cependant, même en supposant que le juge de première instance détermine correctement la norme juridique à appliquer, il lui est encore possible de commettre une erreur lorsqu'il apprécie les faits à la lumière de cette norme juridique. Par exemple, il peut exister une preuve indiquant qu'un accident s'était déjà produit sur le tronçon de chemin en cause. Le juge de première instance qui se demande si ce fait satisfait ou non au critère juridique applicable à la question de la connaissance doit poser un certain nombre d'hypothèses normatives. Il doit se demander si le fait qu'un accident se soit déjà produit au même endroit alerterait le conseiller municipal moyen, raisonnable et prudent de l'existence d'un danger. Il doit également se demander si ce conseiller aurait appris l'existence de l'accident antérieur par un système d'information sur les accidents. Selon moi, la question de savoir si le fait qu'un accident se soit produit antérieurement

requirement is a question of mixed fact and law and it is artificial to characterize it as anything else. As is apparent from the example given, the question may also raise normative issues which should be reviewable by an appellate court on the correctness standard.

110 I agree with my colleagues that it is not possible to state as a general proposition that all matters of mixed fact and law are reviewable according to the standard of correctness: citing *Southam*, *supra*, at para. 37 (para. 28). I disagree, however, that the dicta in *Southam* establishes that a trial judge's conclusions on questions of mixed fact and law in a negligence action should be accorded deference in every case. This Court in *St-Jean v. Mercier*, [2002] 1 S.C.R. 491, 2002 SCC 15, a medical negligence case, distinguished *Southam* on the issue of the standard applicable to questions of mixed fact and law where the tribunal has no particular expertise. Gonthier J., writing for a unanimous Court, stated at paras. 48-49:

> A question "about whether the facts satisfy the legal tests" is one of mixed law and fact. Stated differently, "whether the defendant satisfied the appropriate standard of care is a question of mixed law and fact" (*Southam*, at para. 35).
>
> Generally, such a question, once the facts have been established without overriding and palpable error, is to be reviewed on a standard of correctness since the standard of care is normative and is a question of law within the normal purview of both the trial and appellate courts. Such is the standard for medical negligence. There is no issue of expertise of a specialized tribunal in a particular field which may go to the determination of facts and be pertinent to defining an appropriate standard and thereby call for some measure of deference by a court of general appeal (*Southam*, *supra*, at para. 45; and *Nova Scotia Pharmaceutical Society*, *supra*, at p. 647).

111 I also disagree with my colleagues that *Jaegli Enterprises Ltd. v. Taylor*, [1981] 2 S.C.R. 2, is authority for the proposition that when the question

satisfait à l'exigence de connaissance applicable est une question mixte de fait et de droit, et il serait artificiel de la qualifier autrement. Comme l'indique clairement l'exemple qui précède, cette question peut également soulever des questions normatives que devrait pouvoir contrôler une cour d'appel selon la norme de la décision correcte.

Je partage l'opinion de mes collègues selon laquelle on ne peut poser comme principe général que toutes les questions mixtes de fait et de droit sont assujetties à la norme de la décision correcte : citant *Southam*, précité, par. 37 (par. 28). Cependant, je ne crois pas que l'opinion formulée dans *Southam* signifie que, dans une affaire de négligence, les conclusions du juge de première instance sur des questions mixtes de fait et de droit commandent systématiquement une attitude empreinte de retenue. Dans l'arrêt *St-Jean c. Mercier*, [2002] 1 R.C.S. 491, 2002 CSC 15, affaire de négligence médicale, notre Cour a différencié cette affaire de l'arrêt *Southam* sur la question de la norme de contrôle applicable aux questions mixtes de fait et de droit dans les cas où le tribunal ne possède d'expertise particulière. Exposant la décision unanime de la Cour, le juge Gonthier a dit ceci, aux par. 48 et 49 :

> La question qui consiste « à déterminer si les faits satisfont au critère juridique » est une question mixte de droit et de fait ou en d'autres termes, « la question de savoir si le défendeur a respecté la norme de diligence appropriée est une question de droit et de fait » (*Southam*, par. 35).
>
> Une fois les faits établis sans erreur manifeste et dominante, cette question doit généralement être révisée suivant la norme de la décision correcte puisque la norme de diligence est normative et constitue une question de droit qui relève de la compétence habituelle des tribunaux de première instance et d'appel. C'est la norme applicable à la négligence médicale. Il n'est pas question de l'expertise d'un tribunal spécialisé dans un domaine particulier, pouvant toucher la détermination des faits et avoir une incidence sur la définition de la norme appropriée et exiger de ce fait une certaine déférence de la part d'une cour générale d'appel (*Southam*, par. 45; *Nova Scotia Pharmaceutical Society*, précité, p. 647).

Je ne peux non plus me ranger à l'avis de mes collègues selon lequel l'arrêt *Jaegli Enterprises Ltd. c. Taylor*, [1981] 2 R.C.S. 2, permet d'affirmer

of mixed fact and law at issue is a finding of negligence, that finding should be deferred to by appellate courts. In that case the trial judge found that the conduct of the defendant ski instructor met the standard of care expected of him. Moreover, the trial judge found that the accident would have occurred regardless of what the ski instructor had done (*Taylor v. The Queen in Right of British Columbia* (1978), 95 D.L.R. (3d) 82). Seaton J.A. of the British Columbia Court of Appeal disagreed with the trial judge that the ski instructor had met the applicable standard of care (*Taylor (Guardian ad litem of) v. British Columbia* (1980), 112 D.L.R. (3d) 297). Seaton J.A. recognized nevertheless that the "final question" was whether "the instructor's failure to remain was a cause of the accident" (p. 307). On the issue of causation, a question of fact, Seaton J.A. clearly substituted his opinion for that of the trial judge's without regard to the appropriate standard of review. His concluding remarks on the issue of causation at p. 308 highlight his lack of deference to the trial judge's conclusion on causation:

> On balance, I think that the evidence supports the plaintiffs' claim against the instructor, that his conduct in leaving the plaintiff below the crest was one of the causes of the accident.

This Court, which restored the finding of the trial judge, did not clearly state whether it did so on the basis that the appellate court was wrong to interfere with the trial judge's finding of negligence or whether it did so because the appellate court wrongly interfered with the trial judge's conclusions on causation. The reasons suggest the latter. The only portion of the trial judgment that this Court referred to was the finding on causation. Dickson J. (as he then was) remarks in *Jaegli Enterprises*, *supra*, at p. 4:

> At the end of a nine-day trial Mr. Justice Meredith, the presiding judge, delivered a judgment in which he

que, lorsque la question mixte de fait et de droit en litige est la conclusion de négligence tirée par le juge de première instance, les cours d'appel doivent faire preuve de retenue à l'égard de cette conclusion. Dans cette affaire, le juge de première instance avait conclu que le défendeur, un instructeur de ski, avait respecté la norme de diligence à laquelle il était tenu. Il avait aussi conclu que l'accident serait survenu, indépendamment de la conduite de l'instructeur de ski (*Taylor c. The Queen in Right of British Columbia* (1978), 95 D.L.R. (3d) 82). Le juge Seaton de la Cour d'appel de la Colombie-Britannique a exprimé son désaccord avec la conclusion du juge de première instance que l'instructeur de ski avait respecté la norme de diligence applicable (*Taylor (Guardian ad litem of) c. British Columbia* (1980), 112 D.L.R. (3d) 297). Il a néanmoins reconnu que [TRADUCTION] « l'ultime question » consistait à se demander si « l'omission de l'instructeur de rester près de la demanderesse avait été une cause de l'accident » (p. 307). Sur la question du lien de causalité, qui est une question de fait, le juge Seaton a clairement substitué son opinion à celle du juge de première instance sans tenir compte de la norme de contrôle appropriée. Ses remarques finales sur la question de la causalité, à la p. 308, font ressortir son absence de retenue à l'égard de la conclusion du juge de première instance sur ce point :

> [TRADUCTION] Tout bien considéré, j'estime que la preuve étaye la prétention des demandeurs voulant que la conduite de l'instructeur, qui l'a laissée seule sous la crête de la butte, a été l'une des causes de l'accident.

112 En rétablissant la décision du juge de première instance, notre Cour n'a pas précisé si elle le faisait parce que la cour d'appel avait eu tort de modifier la conclusion de ce dernier sur la négligence ou parce qu'elle avait erronément modifié ses conclusions sur la causalité. Les motifs donnent à penser que la dernière proposition est la bonne. La seule partie du jugement de première instance mentionnée par notre Cour se rapporte à la conclusion sur le lien de causalité. Le juge Dickson (plus tard Juge en chef) a fait les remarques suivantes dans l'arrêt *Jaegli Enterprises*, précité, à la p. 4 :

> À la fin d'un procès de neuf jours, le juge Meredith, qui a présidé le procès, a rendu un jugement dans lequel il a

very carefully considered all of the evidence and concluded that the accident had been caused solely by Larry LaCasse and that the plaintiffs should recover damages, in an amount to be assessed, against LaCasse. The claims against Paul Ankenman, Jaegli Enterprises Limited and the other defendants were dismissed with costs.

113 The Court went on to cite a number of cases, some of which did not involve negligence (see *Schreiber Brothers Ltd. v. Currie Products Ltd.*, [1980] 2 S.C.R. 78), for the general proposition that "it [is] wrong for an appellate court to set aside a trial judgment where [there is not palpable and overriding error, and] the only point at issue [was] the interpretation of the evidence as a whole" (p. 84). Given that the Court focussed on the issue of causation, a question of fact alone, I do not think that *Jaegli Enterprises* establishes that a finding of negligence by the trial judge should be deferred to by appellate courts. In my view, the Court in *Jaegli Enterprises* merely affirmed the longstanding principle that an appellate court should not interfere with a trial judge's finding of fact absent a palpable and overriding error.

(2) Error of Law in the Reasons of the Court of Queen's Bench

114 The standard of care set out in s. 192 of *The Rural Municipality Act, 1989*, as interpreted within the jurisprudence, required the trial judge to examine whether the portion of Snake Hill Road on which the accident occurred posed a hazard to the reasonable driver exercising ordinary care. Having identified the correct legal test, the trial judge nonetheless failed to ask herself whether a reasonable driver exercising ordinary care would have been able to safely drive the portion of the road on which the accident occurred. To neglect entirely one branch of a legal test when applying the facts to the test is to misconstrue the law (*Southam*, *supra*, at para. 39). The Saskatchewan Court of Appeal was therefore right to characterize this failure as an error of law and to consider the factual findings made by the trial judge in light of the appropriate legal test.

examiné soigneusement toute la preuve et a conclu que l'accident était imputable uniquement à Larry LaCasse et que les demandeurs pouvaient recouvrer de LaCasse des dommages-intérêts pour un montant à déterminer. Les réclamations contre Paul Ankenman, Jaegli Enterprises Limited et les autres défendeurs ont été rejetées avec dépens.

La Cour a ensuite cité quelques décisions, dont certaines ne traitent pas de négligence (voir *Schreiber Brothers Ltd. c. Currie Products Ltd.*, [1980] 2 R.C.S. 78), au soutien de la proposition générale qu'« une cour d'appel ne peut à bon droit infirmer une décision de première instance lorsque la seule question en litige porte sur l'interprétation de l'ensemble de la preuve » (p. 84). Étant donné que la Cour s'est attachée à la question du lien de causalité, question de fait seulement, je ne crois pas que l'arrêt *Jaegli Enterprises* établisse que les cours d'appel doivent faire montre de retenue lorsque le juge de première instance conclut à la négligence. À mon avis, dans l'arrêt *Jaegli Enterprises*, la Cour n'a fait que confirmer le principe bien établi portant qu'une cour d'appel ne doit pas modifier une conclusion de fait du juge de première instance en l'absence d'erreur manifeste et dominante.

(2) L'erreur de droit dans les motifs de la Cour du Banc de la Reine

Suivant la norme de diligence énoncée à l'art. 192 de la *Rural Municipality Act, 1989*, telle qu'elle a été interprétée dans la jurisprudence, la juge de première instance devait se demander si le tronçon du chemin Snake Hill sur lequel s'est produit l'accident constituait un danger pour le conducteur raisonnable prenant des précautions normales. Après avoir déterminé quel était le critère juridique applicable, la juge de première instance a toutefois omis de se demander si un tel conducteur aurait pu rouler en sécurité sur le tronçon en question. Le fait d'omettre entièrement une étape d'un critère juridique, dans l'application de celui-ci aux faits de l'espèce, équivaut à mal interpréter le droit (*Southam*, précité, par. 39). Par conséquent, la Cour d'appel de la Saskatchewan a donc eu raison de qualifier cette omission d'erreur de droit et de contrôler les conclusions de fait tirées par la juge de première instance à la lumière du critère juridique approprié.

The long line of jurisprudence interpreting s. 192 of *The Rural Municipality Act, 1989* and its predecessor provisions clearly establishes that the duty of the municipality is to keep the road "in such a reasonable state of repair that those requiring to use it may, exercising ordinary care, travel upon it with safety" (*Partridge*, *supra*, at p. 558; *Levey v. Rural Municipality of Rodgers, No. 133*, [1921] 3 W.W.R. 764 (Sask. C.A.), at p. 766; *Diebel Estate v. Pinto Creek No. 75 (Rural Municipality)* (1996), 149 Sask. R. 68 (Q.B.), at pp. 71-72). Legislation in several other provinces establishes a similar duty of care and courts in these provinces have interpreted it in a similar fashion (*R. v. Jennings*, [1966] S.C.R. 532, at p. 537; *County of Parkland No. 31 v. Stetar*, [1975] 2 S.C.R. 884, at p. 892; *Fafard v. City of Quebec* (1917), 39 D.L.R. 717 (S.C.C.), at p. 718). This Court, in *Jennings*, *supra*, interpreting a similar provision under the Ontario *Highway Improvement Act*, R.S.O. 1960, c. 171, remarked at p. 537 that: "[i]t has been repeatedly held in Ontario that where a duty to keep a highway in repair is imposed by statute the body upon which it is imposed must keep the highway in such a condition that travellers using it with ordinary care may do so with safety".

115 La jurisprudence de longue date portant sur l'interprétation de l'art. 192 de la *Rural Municipality Act, 1989* et des dispositions qu'il a remplacées établit clairement que les municipalités ont l'obligation de tenir les chemins [TRADUCTION] « dans un état raisonnable d'entretien de façon que ceux qui doivent l[es] emprunter puissent, en prenant des précautions normales, y circuler en sécurité » (*Partridge*, précité, p. 558; *Levey c. Rural Municipality of Rodgers, No. 133*, [1921] 3 W.W.R. 764 (C.A. Sask.), p. 766; *Diebel Estate c. Pinto Creek No. 75 (Rural Municipality)* (1996), 149 Sask. R. 68 (B.R.), p. 71 et 72). Plusieurs autres provinces ont adopté des lois établissant une obligation de diligence semblable, et les tribunaux de ces provinces ont interprété cette obligation de la même façon (*R. c. Jennings*, [1966] R.C.S. 532, p. 537; *Comté de Parkland nº 31 c. Stetar*, [1975] 2 R.C.S. 884, p. 892; *Fafard c. City of Quebec* (1917), 39 D.L.R. 717 (C.S.C.), p. 718). Interprétant une disposition similaire de la *Highway Improvement Act* de l'Ontario, R.S.O. 1960, ch. 171, notre Cour a indiqué, dans l'arrêt *Jennings*, précité, p. 537, qu'[TRADUCTION] « [i]l a été décidé à maintes reprises en Ontario que, lorsque l'obligation de maintenir une route en bon état d'entretien est légalement imposée à un organisme, celui-ci doit maintenir la route dans un état permettant à ceux qui l'empruntent en prenant des précautions normales d'y circuler en sécurité ».

There is good reason for limiting the municipality's duty to repair to a standard which permits drivers exercising ordinary care to proceed with safety. As stated by this Court in *Fafard*, *supra*, at p. 718: "[a] municipal corporation is not an insurer of travellers using its streets; its duty is to use reasonable care to keep its streets in a reasonably safe condition for ordinary travel by persons exercising ordinary care for their own safety". Correspondingly, appellate courts have long held that it is an error for the trial judge to find a municipality in breach of its duty merely because a danger exists, regardless of whether or not that danger poses a risk to the ordinary user of the road. The type of error to be guarded against was described by Wetmore C.J. in *Williams v.*

116 Il existe de bonnes raisons de limiter l'obligation d'entretien des routes incombant aux municipalités au respect d'une norme suffisante pour permettre aux conducteurs qui prennent des précautions normales d'y circuler en sécurité. Comme l'a dit notre Cour dans l'arrêt *Fafard*, précité, p. 718 : [TRADUCTION] « [l]es municipalités ne sont pas les assureurs des automobilistes qui roulent dans leurs rues; leur obligation consiste à faire preuve de diligence raisonnable et de maintenir leurs rues dans un état raisonnablement sécuritaire pour la circulation normale des personnes qui prennent des précautions normales en vue d'assurer leur propre sécurité ». En conséquence, les cours d'appel estiment depuis longtemps que le juge de première instance commet une erreur s'il conclut qu'une municipalité

Town of North Battleford (1911), 4 Sask. L.R. 75 (*en banc*), at p. 81:

> The question in an action of this sort, whether or not the road is kept in such repair that those requiring to use it may, using ordinary care, pass to and fro upon it in safety, is, it seems to me, largely one of fact . . . I would hesitate about setting aside a finding of fact of the trial Judge if he had found the facts necessary for the determination of the case, but he did not so find. He found that the crossing was a "dangerous spot without a light, and that if the utmost care were used no accident might occur, but it was not in such proper or safe state as to render such accident unlikely to occur." He did not consider the question from the standpoint of whether or not those requiring to use the road might, using ordinary care, pass to and fro upon it in safety. The mere fact of the crossing being dangerous is not sufficient . . . . [Emphasis added.]

117 From the jurisprudence cited above, it is clear that the mere existence of a hazard or danger does not in and of itself give rise to a duty on the part of the municipality to erect a sign. Even if a trial judge concludes on the facts that the conditions of the road do, in fact, present a hazard, he or she must still go on to assess whether that hazard would present a risk to the reasonable driver exercising ordinary care. The ordinary driver is often faced with inherently dangerous driving conditions. Motorists drive in icy or wet conditions. They drive at night on country roads that are not well lit. They are faced with obstacles such as snow ridges and potholes. These obstacles are often not in plain view, but are obscured or "hidden". Common sense dictates that motorists will, however, exercise a degree of caution when faced with dangerous driving conditions. A municipality is expected to provide extra cautionary measures only where the conditions of the road and the surrounding circumstances do not signal to the driver the possibility that a hazard is present. For example, the ordinary driver expects a dirt road to become slippery when wet. By contrast, paved

manque à son obligation du seul fait qu'un danger existe, indépendamment de la question de savoir si ce danger présente ou non un risque pour l'usager ordinaire du chemin. Le genre d'erreur qu'il faut éviter a été décrit ainsi par le juge en chef Wetmore dans l'affaire *Williams c. Town of North Battleford* (1911), 4 Sask. L.R. 75 (*in banco*), p. 81 :

> [TRADUCTION] Il me semble que la question qui se pose dans ce genre d'action — soit celle de savoir si le chemin est tenu dans un état d'entretien tel que ceux qui doivent l'emprunter puissent, en prenant des précautions normales, y circuler en sécurité — est essentiellement une question de fait [. . .] j'hésiterais à écarter une conclusion de fait du juge de première instance s'il avait relevé l'existence des faits nécessaires pour trancher l'affaire, mais il ne l'a pas fait. Il a conclu que l'intersection était « un endroit dangereux non éclairé, et qu'aucun accident ne s'y produirait si on faisait preuve d'une prudence extrême, mais que cet endroit n'était pas tenu dans un état d'entretien propre à rendre improbable un tel accident ». Il n'a pas examiné la question en se demandant si ceux qui doivent emprunter ce chemin peuvent, en prenant des précautions normales, y circuler en sécurité. Le seul fait que l'intersection soit dangereuse n'est pas suffisant . . . [Je souligne.]

Il ressort clairement de la jurisprudence susmentionnée que la simple existence d'un risque ou danger ne fait pas en soi naître pour la municipalité l'obligation d'installer un panneau de signalisation. Même si, à partir des faits, le juge de première instance arrive à la conclusion que l'état du chemin crée effectivement un risque, il doit poursuivre son analyse et se demander si ce risque présente un danger pour le conducteur raisonnable prenant des précautions normales. Le conducteur moyen rencontre souvent des conditions de conduite intrinsèquement dangereuses. Les automobilistes conduisent leur véhicule sur des chaussées glacées ou humides. Ils roulent la nuit sur des chemins de campagne mal éclairés. Ils rencontrent des obstacles comme des bancs de neige et des nids-de-poule. Souvent ces obstacles ne sont pas visibles, car ils sont dissimulés ou « cachés ». Le bon sens suggère que les automobilistes font toutefois preuve d'une certaine prudence en présence de conditions de conduite dangereuses. On n'attend de la municipalité qu'elle prenne des mesures d'avertissement supplémentaires que lorsque l'état du chemin et l'ensemble des

bridge decks on highways are often slick, though they appear completely dry. Consequently, signs will be posted to alert drivers to this unapparent possibility.

autres circonstances ne signalent pas au conducteur la possibilité qu'un danger existe. Par exemple, le conducteur moyen s'attend à ce qu'un chemin de terre devienne glissant lorsqu'il est mouillé. À l'opposé, les tabliers de pont asphaltés qui se trouvent sur les routes sont souvent glissants, bien qu'ils paraissent complètement secs. Par conséquent, des panneaux sont installés pour alerter les conducteurs de cette possibilité non apparente.

The appellant in this case argued, at para. 27 of his factum, that the trial judge did, in fact, assess whether a reasonable driver using ordinary care would find the portion of Snake Hill Road on which the accident occurred to pose a risk. He points in particular to the trial judge's comments at paras. 85-86 that:

> There is a portion of Snake Hill Road that is a hazard to the public. In this regard I accept the evidence of Mr. Anderson and Mr. Werner. Further, it is a hazard that is not readily apparent to users of the road. It is a hidden hazard. . . .
>
> . . . where the existence of . . . bush obstructs the ability of a motorist to be forewarned of a hazard such as that on Snake Hill Road, it is reasonable to expect the R.M. to erect and maintain a warning or regulatory sign so that a motorist, using ordinary care, may be forewarned, adjust speed and take corrective action in advance of entering a dangerous situation. [Emphasis added.]

118 En l'espèce, l'appelant a plaidé, au par. 27 de son mémoire, que la juge de première instance s'était, en fait, demandé si un conducteur raisonnable prenant des précautions normales considérerait que le tronçon du chemin Snake Hill où s'est produit l'accident constitue un risque. Il souligne en particulier les commentaires suivants de la juge de première instance, aux par. 85 et 86 :

> [TRADUCTION] Il y a, sur le chemin Snake Hill, un tronçon qui présente un danger pour le public. À cet égard, je retiens les témoignages de MM. Anderson et Werner. En outre, il s'agit d'un danger qui n'est pas facilement décelable par les usagers du chemin. Il s'agit d'un danger caché . . .
>
> . . . à l'endroit où la présence des broussailles empêche les automobilistes de voir venir un danger comme celui qui existe sur le chemin Snake Hill, il est raisonnable de s'attendre à ce que la M.R. installe et maintienne un panneau d'avertissement ou de signalisation afin qu'un automobiliste prenant des précautions normales soit prévenu et puisse réduire sa vitesse et prendre des mesures correctives avant d'arriver à l'endroit dangereux. [Je souligne.]

The appellant's argument suggests that the trial judge discharged her duty to apply the facts to the law merely by restating the facts of the case in the language of the legal test. This was not, however, sufficient. Although it is clear from the citation above that the trial judge made a factual finding that the portion of Snake Hill Road on which the accident occurred presented drivers with a hidden hazard, there is nothing in this portion of her reasons to suggest that she considered whether or not that portion of the road would pose a risk to the reasonable driver exercising ordinary care. The finding that a hazard, or even that a hidden hazard, exists does not automatically give rise to the conclusion that the reasonable driver exercising ordinary care could not

119 L'appelant semble prétendre que la juge de première instance s'est acquittée de son devoir d'appliquer le droit aux faits simplement en intégrant les faits de l'espèce à la formulation du critère juridique. Ce n'était toutefois pas suffisant. Bien qu'il ressorte clairement des passages précités que la juge de première instance a, à partir des faits, conclu que la portion du chemin Snake Hill où s'est produit l'accident exposait les conducteurs à un danger caché, il n'y a rien dans cette partie de ses motifs qui indique qu'elle s'est demandé si cette portion du chemin présentait un risque pour le conducteur raisonnable prenant des précautions normales. Le fait de conclure à l'existence d'un danger, même caché, n'implique pas forcément que le conducteur

travel through it safely. A proper application of the test demands that the trial judge ask the question: "How would a reasonable driver have driven on this road?" Whether or not a hazard is "hidden" or a curve is "inherently" dangerous does not dispose of the question. My colleagues state that it was open to the trial judge to draw an inference of knowledge of the hazard simply because the sharp curve was a permanent feature of the road (para. 61). Here again, there is nothing in the reasons of the trial judge to suggest that she drew such an inference or to explain how such an inference accorded with the legal requirements concerning the duty of care.

120 Nor did the trial judge consider the question in any other part of her reasons. Her failure to do so becomes all the more apparent when her analysis (or lack thereof) is compared to that in cases in which the courts applied the appropriate method. The Court of Appeal referred to two such cases by way of example. In *Nelson v. Waverley (Rural Municipality)* (1988), 65 Sask. R. 260 (Q.B.), the plaintiff argued that the defendant municipality should have posted signs warning of a ridge in the middle of the road that resulted from the grading of the road by the municipality. The trial judge concluded that if the driver had exercised ordinary care, he could have travelled along the roadway with safety. Instead, he drove too fast and failed to keep an adequate lookout considering the maintenance that was being performed on the road. In *Diebel Estate*, *supra*, the issue was whether the municipality had a duty under s. 192 to post a sign warning motorists that a rural road ended abruptly in a T-intersection. The question of how a reasonable driver exercising ordinary care would have driven on that road was asked and answered by the trial judge in the following passage at p. 74:

His [the expert's] conclusions as to stopping are, however, mathematically arrived at and never having been on

raisonnable prenant des précautions normales ne peut pas y circuler en sécurité. Pour bien appliquer le critère juridique, le juge de première instance doit se poser la question suivante : « Comment un conducteur raisonnable aurait-il roulé sur ce chemin? » Le fait de conclure qu'il existe ou non un danger « caché » ou qu'une courbe est quelque chose d' « intrinsèquement » dangereux ne vide pas la question. Mes collègues affirment que la juge de première instance pouvait inférer la connaissance du danger du seul fait que la courbe serrée constituait une caractéristique permanente du chemin (par. 61). Ici encore, rien dans les motifs de la juge de première instance n'indique qu'elle a tiré une telle inférence ou n'explique en quoi une telle inférence satisfaisait aux conditions juridiques relatives à l'obligation de diligence.

La juge de première instance n'a pas non plus examiné cette question ailleurs dans ses motifs. Son omission à cet égard devient encore plus évidente lorsqu'on compare son analyse (ou son absence d'analyse) à celle des affaires où les tribunaux ont appliqué la bonne démarche. La Cour d'appel a donné comme exemple deux de ces affaires. Dans *Nelson c. Waverley (Rural Municipality)* (1988), 65 Sask. R. 260 (B.R.), le demandeur prétendait que la municipalité défenderesse aurait dû installer des panneaux signalant la présence, au milieu du chemin, d'un sillon résultant de travaux municipaux de nivellement. Le juge de première instance a estimé que, si le conducteur avait pris des précautions normales, il aurait pu rouler en sécurité sur la chaussée. Au lieu de cela, il a roulé trop vite et manqué de vigilance compte tenu des travaux d'entretien qui étaient effectués sur le chemin. Dans *Diebel Estate*, précité, il s'agissait de déterminer si la municipalité avait, en vertu de l'art. 192, l'obligation d'installer un panneau avertissant les automobilistes qu'une route rurale se terminait de façon abrupte à un croisement en T. Le juge de première instance s'est demandé comment un conducteur raisonnable prenant des précautions normales aurait roulé sur ce chemin, et il a répondu ainsi à cette question, à la p. 74 :

[TRADUCTION] Ses conclusions [celles de l'expert] pour ce qui concerne l'arrêt des automobiles découlent

the road, from what was described in the course of the trial, I would think the intersection could be a danger at night to a complete stranger to the area, depending on one's reaction time and the possibility of being confused by what one saw rather than recognizing the T intersection to be just that. On the other hand I would think a complete stranger in the area would be absolutely reckless to drive down a dirt road of the nature of this particular road at night at 80 kilometres per hour. [Emphasis added; emphasis in original deleted.]

The conclusion that Wright J. erred in failing to apply a required aspect of the legal test does not automatically lead to a rejection of her factual findings. This Court's jurisdiction to review questions of law entitles it, where an error of law has been found, to take the factual findings of the trial judge as they are, and to assess these findings anew in the context of the appropriate legal test.

In my view, neither Wright J.'s factual findings nor any other evidence in the record that she might have considered had she asked the appropriate question, support the conclusion that the respondent was in breach of its duty. The portion of Snake Hill Road on which the accident occurred did not pose a risk to a reasonable driver exercising ordinary care because the conditions of Snake Hill Road in general and the conditions with which motorists were confronted at the exact location of the accident signalled to the reasonable motorist that caution was needed. Motorists who appropriately acknowledged the presence of the several factors which called for caution would have been able to navigate safely the so-called "hidden hazard" without the benefit of a road sign.

The question of how a reasonable driver exercising ordinary care would have driven on Snake Hill Road necessitates a consideration of the nature and locality of the road. A reasonable motorist will not approach a narrow gravel road in the country in the same way that he or she will approach a paved highway. It is reasonable to expect a motorist to drive more slowly and to pay greater attention to the potential presence of hazards when driving on a

toutefois d'opérations mathématiques et bien que je n'aie jamais emprunté le chemin en question, d'après les descriptions faites au procès, je suis d'avis que le croisement pourrait constituer un danger la nuit pour quelqu'un qui ne connaît absolument pas l'endroit, eu égard à la vitesse de réaction de chacun et à la possibilité que quelqu'un confonde le croisement en T avec quelque chose d'autre. Par ailleurs, j'estime que quelqu'un ne connaissant aucunement l'endroit agirait de façon tout à fait téméraire en roulant à 80 kilomètres à l'heure la nuit sur un chemin de terre comme celui qui nous intéresse. [Je souligne; soulignement dans l'original omis.]

121 Le fait de conclure que la juge Wright a commis une erreur de droit en omettant d'appliquer un élément essentiel du critère juridique n'invalide pas forcément ses conclusions de fait. En effet, la compétence de notre Cour en matière d'examen des questions de droit l'autorise, lorsqu'une telle erreur est décelée, à reprendre telles quelles les conclusions de fait du juge de première instance et à les réévaluer au regard du critère juridique approprié.

122 Selon moi, ni les faits retenus par la juge Wright ni aucun autre élément de preuve au dossier qu'elle aurait pu prendre en considération si elle s'était posé la bonne question n'appuient sa conclusion que l'intimée a manqué à son obligation. La portion du chemin Snake Hill où s'est produit l'accident ne présentait pas de risque pour un conducteur raisonnable prenant des précautions normales, car l'état de ce chemin en général et les conditions auxquelles les automobilistes doivent faire face à l'endroit précis de l'accident avertissent l'automobiliste raisonnable que la prudence s'impose. Les automobilistes sachant reconnaître les divers facteurs qui appellent à la prudence auraient pu franchir le soi-disant [TRADUCTION] « danger caché » sans l'aide d'un panneau de signalisation.

123 Pour savoir comment un conducteur raisonnable prenant des précautions normales aurait conduit son véhicule sur le chemin Snake Hill, il faut tenir compte de la nature du chemin et de la configuration des lieux. Un automobiliste raisonnable ne roulera pas sur une étroite route de campagne gravelée de la même façon que sur une route asphaltée. Il est raisonnable de s'attendre à ce qu'un automobiliste conduise moins vite et soit plus attentif à la présence

road that is of a lower standard, particularly when he or she is unfamiliar with it.

124 While the trial judge in this case made some comments regarding the nature of the road, I agree with the Court of Appeal's findings that "[s]he might have addressed the matter more fully, taking into account more broadly the terrain through which the road passed, the class and designation of the road in the scheme of classification, and so on . . . " (para. 55). Instead, the extent of her analysis of the road was limited to the following comments, found at para. 84 of her reasons:

> Snake Hill Road is a low traffic road. It is however maintained by the R.M. so that it is passable year round. There are permanent residences on the road. It is used by farmers for access to their fields and cattle. Young people frequent Snake Hill Road for parties and as such the road is used by those who may not have the same degree of familiarity with it as do residents.

125 In my view, the question of how the reasonable driver would have negotiated Snake Hill Road necessitated a somewhat more in-depth analysis of the character of the road. The trial judge's analysis focussed almost entirely on the use of the road, without considering the sort of conditions it presented to drivers. It is perhaps not surprising that the trial judge did not engage in this fuller analysis, given that she did not turn her mind to the question of how a reasonable driver would have approached the road. Had she considered this question, she likely would have engaged in the type of assessment that was made by the Court of Appeal at para. 13 of its judgment:

> The road, about 20 feet in width, was classed as "a bladed trail," sometimes referred to as "a land access road," a classification just above that of "prairie trail". As such, it was not built up, nor gravelled, except lightly at one end of it, but simply bladed across the terrain following the path of least resistance. Nor was it in any way signed.

de dangers potentiels sur un chemin de catégorie inférieure, particulièrement s'il n'est pas familier avec celui-ci.

Bien que, en l'espèce, la juge de première instance ait fait certains commentaires sur la nature du chemin, je souscris à la conclusion de la Cour d'appel selon laquelle [TRADUCTION] « [e]lle aurait pu examiner la question de manière plus approfondie, en tenant davantage compte du type de terrain que le chemin traversait, de la nature et de la désignation du chemin selon le système de classification des routes et ainsi de suite . . . » (par. 55). Au lieu de cela, son analyse s'est limitée aux commentaires suivants, au par. 84 de ses motifs :

> [TRADUCTION] Le chemin Snake Hill est un chemin à faible débit de circulation. Il est néanmoins entretenu par la M.R. à longueur d'année afin de le garder carrossable. Des résidences permanentes sont situées en bordure de celui-ci. Les fermiers l'utilisent pour accéder à leurs champs et à leur bétail. Des jeunes gens empruntent le chemin Snake Hill pour se rendre à des fêtes, de sorte qu'il est utilisé par des conducteurs qui ne le connaissent pas toujours aussi bien que les résidents de l'endroit.

À mon avis, la question de savoir comment un conducteur raisonnable aurait roulé sur le chemin Snake Hill nécessitait un examen un peu plus approfondi de la nature du chemin. Dans son analyse, la juge de première instance s'est attachée presque exclusivement à l'utilisation qui est faite du chemin, sans prendre en compte le genre de conditions qu'il présente aux conducteurs. Il n'est peut-être pas surprenant qu'elle ne se soit pas livrée à cette analyse approfondie, puisqu'elle ne s'est pas demandé comment un conducteur raisonnable aurait roulé sur ce chemin. Si elle s'était posé cette question, elle aurait vraisemblablement procédé à une évaluation analogue à celle qu'a faite la Cour d'appel au par. 13 de son jugement :

> [TRADUCTION] Le chemin, d'une largeur de 20 pieds environ, a été qualifié de « chemin nivelé », qu'on appelle aussi parfois « chemin d'accès », soit tout juste une catégorie au-dessus d'un « chemin de prairie ». Comme tel, il n'a été ni renforcé ni revêtu de gravier, sauf légèrement à l'une de ses extrémités, il s'agit tout simplement d'un chemin nivelé à même le terrain, suivant le tracé présentant le mois d'obstacles. On n'y a installé aucune signalisation.

Given the fact that Snake Hill Road is a low standard road, in a category only one or two levels above a prairie trail, one can assume that a reasonable driver exercising ordinary care would approach the road with a certain degree of caution.

Comme le chemin Snake Hill est une route de catégorie inférieure, à peine un ou deux niveaux au-dessus d'un chemin de prairie, on peut présumer qu'un conducteur raisonnable prenant des précautions normales y roulerait avec une certaine prudence.

Having considered the character of the road in general, and having concluded that by its very nature it warranted a certain degree of caution, it is nonetheless necessary to consider the material features of the road at the point at which the accident occurred. Even on roads which are of a lower standard, a reasonable driver exercising due caution may be caught unaware by a particularly dangerous segment of the road. That was, in fact, the central argument that the appellant put forward in this case. According to the appellant's "dual nature" theory, at para. 8 of his factum, the fact that the curvy portion of Snake Hill Road where the accident occurred was flanked by straight segments of road created a risk that a motorist would be lulled into thinking that the curves could be taken at speeds greater than that at which they could actually be taken.

126 Après avoir examiné la nature générale du chemin et avoir conclu que, du fait de cette nature même, une certaine prudence s'imposait, il faut néanmoins prendre en considération les caractéristiques physiques du chemin à l'endroit où l'accident s'est produit. Même sur des chemins de catégorie inférieure, un conducteur raisonnable prenant des précautions normales pourrait être pris par surprise sur un tronçon particulièrement dangereux. Il s'agit là, en fait, de l'argument central présenté par l'appelant en l'espèce. Selon sa thèse, dite de la « nature hybride » du chemin, au par. 8 de son mémoire, le fait que la courbe où est survenu l'accident se trouve entre des tronçons en ligne droite risquait d'amener les automobilistes à croire que les virages pouvaient être pris à des vitesses supérieures à celles auxquelles ils pouvaient l'être en réalité.

While it is not clear from her reasons that the trial judge accepted the appellant's "dual nature" theory, it appears that her conclusion that the municipality did not meet the standard of care required by it was based largely on her observation of the material features of the road at the location of the Nikolaisen rollover. Relying on the evidence of two experts, Mr. Anderson and Mr. Werner, she found the portion of the road on which the accident occurred to be a "hazard to the public". In her view, the limited sight distance created by the presence of uncleared bush precluded a motorist from being forewarned of the impending sharp right turn immediately followed by a left turn. Based on expert testimony, she concluded that the curve could not be negotiated at speeds greater than 60 km/h under favourable conditions, or 50 km/h under wet conditions.

127 Bien que les motifs de la juge de première instance n'indiquent pas clairement si elle a retenu la thèse de la « nature hybride » du chemin, il semble que sa conclusion selon laquelle la municipalité a manqué à son obligation d'entretien ait reposé largement sur son examen des caractéristiques physiques du chemin, à l'endroit où le véhicule de M. Nikolaisen a fait un tonneau. S'appuyant sur les témoignages de deux experts, MM. Anderson et Werner, elle a estimé que la portion du chemin où s'est produit l'accident constituait un [TRADUCTION] « danger pour le public ». Selon elle, le fait que la distance de visibilité ait été réduite par la présence de broussailles empêchait les automobilistes de voir l'imminence d'un virage à droite serré, qui est immédiatement suivi d'un virage à gauche. Sur la base des témoignages d'experts, elle a conclu que le virage ne pouvait être pris à une vitesse supérieure à 60 km/h dans des conditions favorables, ou 50 km/h sur chaussée humide.

Again, I would not reject the trial judge's factual finding that the curve presented motorists with an

128 Je ne rejetterais pas, je le répète, la conclusion de fait selon laquelle la courbe présentait un risque

inherent hazard. The evidence does not, however, support a finding that a reasonable driver exercising ordinary care would have been unable to negotiate the curve with safety. As I explained earlier, the municipality's duty to repair is implicated only when an objectively hazardous condition exists, and where it is determined that a reasonable driver arriving at the hazard would be unable to provide for his or her own security due to the features of the hazard.

129 I agree with the trial judge that part of the danger posed by the presence of bushes on the side of the road was that a driver would not be able to predict the radius of the sharp right-turning curve obscured by them. In my view, however, the actual danger inherent in this portion of the road was that the bushes, together with the sharp radius of the curve, prevented an eastbound motorist from being able to see if a vehicle was approaching from the opposite direction. Given this latter situation, it is highly unlikely that any reasonable driver exercising ordinary care would approach the curve at speeds in excess of 50 km/h, a speed which was found by the trial judge to be a safe speed at which to negotiate the curve. Since a reasonable driver would not approach this curve at speeds in excess of which it could safely be taken, I conclude that the curve did not pose a risk to the reasonable driver.

130 One need only refer to the series of photographs of the portion of Snake Hill Road on which the accident occurred to appreciate the extent to which visual clues existed which would alert a driver to approach the curve with caution (Respondent's Record, vol. II, at pp. 373-76). The photographs, which indicate what the driver would have seen on entering the curve, show the presence of bush extending well into the road. From the photographs, it is clear that a motorist approaching the curve would not fail to appreciate the risk presented by the curve, which is simply that it is impossible to see around it and to gauge what may be coming in the opposite direction. In addition, the danger posed

intrinsèque pour les automobilistes. Toutefois, il n'y a rien dans la preuve qui permette de conclure qu'un conducteur raisonnable prenant des précautions normales aurait été incapable de prendre le virage en sécurité. Comme je l'ai expliqué plus tôt, l'obligation d'entretien des municipalités n'est en cause que lorsqu'il existe une situation objectivement dangereuse et qu'il est établi qu'un conducteur raisonnable s'approchant du danger serait incapable d'assurer sa sécurité en raison des caractéristiques de ce danger.

Je partage l'opinion de la juge de première instance selon laquelle une partie du danger créé par les broussailles se trouvant en bordure de la route tenait au fait qu'un conducteur ne pourrait deviner le rayon de courbure prononcé du virage à droite serré qu'elles dissimulaient. À mon sens, toutefois, le véritable danger intrinsèque de ce tronçon du chemin résidait dans le fait que les broussailles, ainsi que le court rayon de courbure du virage, empêchent les automobilistes circulant en direction est de voir si un véhicule s'approche en sens inverse. Par conséquent, il est très peu probable qu'un conducteur raisonnable prenant des précautions normales approcherait de ce virage à une vitesse supérieure à 50 km/h, vitesse à laquelle la juge de première instance a conclu qu'il était possible de le prendre en sécurité. Étant donné qu'un conducteur raisonnable n'approcherait pas de ce virage à une vitesse supérieure à celle lui permettant de le prendre en sécurité, je conclus que le virage ne constituait pas un risque pour le conducteur raisonnable.

Il suffit d'examiner les photos du tronçon du chemin Snake Hill où l'accident est survenu pour constater à quel point il existait des indices visuels propres à inciter les conducteurs à s'approcher du virage avec prudence (dossier de l'intimée, vol. II, p. 373-376). Les photos, qui montrent ce que voit le conducteur sur le point d'amorcer le virage, laissent voir la présence de broussailles s'avançant considérablement au-dessus du chemin. Il ressort clairement de ces photographies qu'un automobiliste approchant du virage ne manquerait pas pressentir le risque que présente celui-ci, savoir qu'il est tout simplement impossible de voir de l'autre côté de la courbe ce qui peut arriver en sens inverse. De plus,

by the inability to see what is approaching in the opposite direction is somewhat heightened by the fact that this road is used by farm operators. At trial, the risk was described in the following terms by Mr. Sparks, an engineer giving expert testimony:

> . . . if you can't, if you can't see far enough down the road to, you know, if there's somebody that's coming around the corner with a tractor and a cultivator and you can't see around the corner, then, you know, drivers would have a fairly strong signal, in my view, that due care and caution would be required.

The expert testimony relied on by the trial judge does not support a finding that the portion of Snake Hill Road on which the accident occurred would pose a risk to a reasonable driver exercising ordinary care. When asked at trial whether motorists, exercising reasonable care, would enter the curve at a slow speed because they could not see what was coming around the corner, Mr. Werner agreed that he, himself, drove the corner "at a slower speed" and that it would be prudent for a driver to slow down given the limited sight distance. Similarly, Mr. Anderson admitted to having taken the curve at 40-45 km/h the first time he drove it because he "didn't want to get into trouble with it". When asked if the reason he approached the curve at that speed was because he could not see around it, he replied in the affirmative: "[t]hat's why I approached it the way I did."

Perhaps most tellingly, Mr. Nikolaisen himself testified that he could not see if a vehicle was coming in the opposite direction as he approached the curve. The following exchange which occurred during counsel's cross-examination of Mr. Nikolaisen at trial is instructive:

> Q. . . . You told my learned friend, Mr. Logue, that your view of the road was quite limited, that is correct? The view ahead on the road is quite limited, is that right?

le danger que constitue l'incapacité de voir ce qui arrive en sens inverse est d'une certaine manière exacerbé par le fait que le chemin est utilisé par des exploitants agricoles. Au procès, ce risque a été décrit ainsi par M. Sparks, ingénieur, qui témoignait à titre d'expert :

> [TRADUCTION] . . . si vous ne pouvez pas voir, si vous ne pouvez pas voir assez loin sur le chemin pour, vous savez, savoir si quelqu'un arrive en sens inverse avec un tracteur tirant une herse et que vous ne pouvez voir, de l'autre côté du virage, alors, vous savez, cela devrait envoyer un message clair aux conducteurs, selon moi, que l'attention et la prudence s'imposent.

131 Le témoignage d'expert retenu par la juge de première instance n'étaye pas sa conclusion que la portion du chemin Snake Hill où s'est produit l'accident présente un risque pour un conducteur raisonnable prenant des précautions normales. Lorsqu'on lui a demandé si un automobiliste prenant des précautions normales amorcerait le virage à vitesse réduite étant donné qu'il ne peut voir ce qui l'attend au détour du chemin, M. Werner a reconnu que lui-même prend le virage [TRADUCTION] « à vitesse réduite » et qu'il serait prudent que les conducteurs ralentissent en raison de la distance de visibilité limitée. De même, M. Anderson a admis avoir pris le virage à 40-45 km/h la première fois qu'il est passé par là, car il [TRADUCTION] « ne voulait pas se placer dans une situation difficile ». Lorsqu'on lui a demandé s'il avait pris le virage à cette vitesse parce qu'il ne pouvait pas voir ce qui l'attendait, il a répondu par l'affirmative : [TRADUCTION] « [c']est la raison pour laquelle je l'ai approché comme je l'ai fait. »

132 Fait encore plus révélateur peut-être, M. Nikolaisen lui-même a témoigné qu'il ne pouvait pas savoir si un véhicule venait en sens inverse lorsqu'il s'approchait du virage. L'échange suivant, durant le contre-interrogatoire de M. Nikolaisen au procès par l'avocat de la partie adverse, est éclairant :

[TRADUCTION]

> Q. . . . Vous avez dit à mon savant collègue, M. Logue, que votre visibilité était plutôt réduite, est-ce exact? La visibilité sur le chemin est plutôt réduite, n'est-ce pas?

A. As in regards to travelling through the curves, yes, that's right, yeah.

Q. Yes. And you did not know what was coming as you approached the curve, that is correct?

A. That's correct, yes.

Q. There might be a vehicle around that curve coming towards you or someone riding a horse on the road, that is correct?

A. Or a tractor or a cultivator or something, that's right.

Q. Or a tractor or a cultivator. You know as a person raised in rural Saskatchewan that all of those things are possibilities, that is right?

A. That's right, yeah, that is correct.

133 Nor do I accept the appellant's submission that the "dual nature" of the road had the effect of lulling drivers into taking the curve at an inappropriate speed. This theory rests on the assumption that the motorists would drive the straight portions of the road at speeds of up to 80 km/h, leaving them unprepared to negotiate suddenly appearing curves. Yet, while the default speed limit on the road was 80 km/h, there was no evidence to suggest that a reasonable driver would have driven any portion of the road at that speed. While Mr. Werner testified that a driver "would be permitted" to drive at a maximum of 80 km/h, since this was the default (not the posted) speed limit, he later acknowledged that bladed trails in the province are not designed to meet 80 km/h design criteria. I agree with the Court of Appeal that the evidence is that "Snake Hill Road was self-evidently a dirt road or bladed trail" and that it "was obviously not designed to accommodate travel at a general speed of 80 kilometres per hour". As I earlier remarked, the locality of the road and its character and class must be considered when determining whether the reasonable driver would be able to navigate it safely.

R. Lorsqu'on se trouve dans les courbes, oui, c'est exact.

Q. Oui. Et vous ne saviez pas ce qui s'en venait lorsque vous approchiez du virage, est-ce exact?

R. C'est exact, oui.

Q. Il aurait pu y avoir un véhicule venant dans votre direction de l'autre côté de la courbe ou quelqu'un se promenant à cheval sur le chemin, est-ce exact?

R. Ou un tracteur, un cultivateur ou autre chose, c'est vrai.

Q. Ou un tracteur ou un cultivateur. Vous savez, puisque vous avez grandi en milieu rural en Saskatchewan, que toutes ces situations sont autant de possibilités, n'est-ce pas?

R. C'est vrai, oui.

Je ne retiens pas non plus l'argument de l'appelant portant que la « nature hybride » du chemin avait pour effet d'amener les conducteurs à prendre le virage à une vitesse inappropriée. Cette théorie repose sur l'hypothèse que les automobilistes roulent sur les portions en ligne droite du chemin à une vitesse pouvant atteindre 80 km/h, et qu'ils se trouvent en conséquence pris de court lorsqu'ils doivent prendre un virage soudain. Pourtant, bien que la vitesse permise sur le chemin soit 80 km/h, rien dans la preuve n'indiquait qu'un conducteur raisonnable aurait roulé à cette vitesse à quelque endroit du chemin. Après avoir témoigné que les conducteurs [TRADUCTION] « étaient autorisés » à rouler à une vitesse maximale de 80 km/h, cette vitesse étant la vitesse permise par défaut (et non la vitesse affichée), M. Werner a reconnu que les chemins nivelés de la province ne sont pas conçus pour permettre la circulation à une vitesse de 80 km/h. À l'instar de la Cour d'appel, je suis d'avis que la preuve établit que [TRADUCTION] « le chemin Snake Hill était manifestement un chemin de terre ou un chemin nivelé » et qu'il « n'était clairement pas conçu pour permettre une vitesse générale de 80 kilomètres à l'heure ». Comme je l'ai souligné précédemment, la configuration du chemin, de même que sa nature et sa catégorie doivent être prises en considération pour décider si le conducteur raisonnable aurait pu y rouler en sécurité.

Furthermore, the evidence at trial did not suggest that drivers were somehow fooled by the so-called "dual nature" of the road. The following exchange between counsel for the respondent and Mr. Werner at trial is illustrative of how motorists would view the road:

Q. Now, Mr. Werner, would you not agree that the change in the character of this road as you proceeded from east to west was quite obvious?

A. It was straight, and then you came to a hill, and you really didn't know what might lie beyond the hill.

Q. That's right. But I mean, the fact that the road went from being straight and level to suddenly there was a hill and you couldn't see -- you could see from the point of the top of the hill that the road didn't continue in a straight line, couldn't you?

A. Yes, you could, from the top of the hill, it's a very abrupt hill, yes.

Q. And as you proceeded down though the hill it became quite obvious, did it not, that the character of the road changed?

A. Yes, it changed, yes.

Q. Now you were faced with something other than a straight road?

A. M'hm. Yes.

Q. Now you were on -- and at some point along there the surface of the road changed, did it not?

A. Yes.

Q. And, of course, the road was no longer, I use the term built-up to refer to a road that has grade and it has some drainage. As you proceeded from west to east, you realized, you could see, it was obvious that this was not longer a built-up road?

A. It was a road essentially that was cut out of the topography and had no ditches, and there was an abutment or shoulder right to the driving surface. It was different than the first part.

Q. Yes. And all those differences were obvious, were they not?

134

En outre, rien dans la preuve présentée au procès n'indiquait que les conducteurs avaient été trompés de quelque façon par la soi-disant « nature hybride » du chemin. L'échange suivant, entre l'avocat de l'intimée et M. Werner, illustre bien la façon dont les automobilistes perçoivent le chemin :

[TRADUCTION]

Q. Maintenant M. Werner, ne seriez-vous pas d'accord pour dire que le changement dans la nature de ce chemin lorsque vous rouliez d'est en ouest était très évident?

R. On roulait en ligne droite, puis on descendait une colline, et on ne savait vraiment pas ce qui pouvait se trouver de l'autre côté de la colline.

Q. C'est vrai. Mais je veux dire, le fait que le chemin suivait d'abord un tracé horizontal et en ligne droite pour soudainement devenir une colline et que vous ne pouviez pas voir -- vous pouviez voir du haut de la colline que le chemin ne continuait pas en ligne droite, n'est-ce pas?

R. Oui, vous pouviez, du haut de la colline, c'est une colline très abrupte, oui.

Q. Et au fur et à mesure que vous descendiez la colline il devenait assez évident, n'est-ce pas, que la nature du chemin changeait?

R. Oui, ça changeait, oui.

Q. Vous vous trouviez alors devant autre chose qu'un chemin en ligne droite?

R. M'hm. Oui.

Q. Vous étiez maintenant sur -- et à un moment donné la surface du chemin changeait, n'est-ce pas?

R. Oui.

Q. Et, évidemment, le chemin n'était plus, j'utilise le terme aménagé pour désigner un chemin possédant une certaine élévation et qui est dans une certaine mesure drainé. Au fur et à mesure que vous rouliez d'ouest en est, vous constatiez, vous pouviez voir, il était évident, qu'il ne s'agissait plus d'un chemin aménagé?

R. Il s'agit essentiellement d'un chemin tracé suivant la topographie des lieux et sans fossés, et il y avait un accotement à droite du conducteur. C'était différent de la portion précédente.

Q. Oui. Et toutes ces différences étaient évidentes, n'est-ce pas?

A. Well, I -- they were clear, satisfactorily clear to me, yes. [Emphasis added.]

135 Although they may be compelling factors in other cases, in this case the "dual nature" of the road, the radius of the curve, the surface of the road, and the lack of superelevation do not support the conclusion of the trial judge. The question of how a reasonable driver exercising ordinary care would approach this road demands common sense. There was no necessity to post a sign in this case for the simple reason that any reasonable driver would have reacted to the presence of natural cues to slow down. The law does not require a municipality to post signs warning motorists of hazards that pose no real risk to a prudent driver. To impose a duty on the municipality to erect a sign in a case such as this is to alter the character of the duty owed by a municipality to drivers. Municipalities are not required to post warnings directed at drunk drivers and thereby deal with their inability to react to the cues that alert the ordinary driver to the presence of a hazard.

136 My colleagues assert that the trial judge properly considered all aspects of the applicable legal test, including whether the curve would pose a risk to the reasonable driver exercising ordinary care. They say that the trial judge did discuss, both explicitly and implicitly, the conduct of an ordinary or reasonable motorist approaching the curve. Secondly, they note that she referred to the evidence of the experts, Mr. Anderson and Mr. Werner, both of whom discussed the conduct of an ordinary motorist in this situation. Thirdly, the fact that the trial judge apportioned negligence to Nikolaisen indicates, in their view, that she assessed his conduct against the standard of the ordinary driver, and thus considered the conduct of the latter (para. 40).

R. Bien, je -- elles étaient évidentes, suffisamment évidentes pour moi, oui. [Je souligne.]

Bien qu'ils puissent constituer des facteurs concluants dans d'autres affaires, la « nature hybride » du chemin, le rayon de courbure du virage, le revêtement du chemin et l'absence d'élévation n'étayent pas en l'espèce la conclusion de la juge de première instance. Pour répondre à la question de savoir comment un conducteur raisonnable prenant des précautions normales roulerait sur ce chemin, il faut faire appel au bon sens. Il n'était pas nécessaire d'installer un panneau de signalisation en l'espèce, et ce pour la simple raison que n'importe quel conducteur raisonnable aurait réagi aux indices naturels l'invitant à ralentir. Le droit n'oblige pas les municipalités à installer des panneaux signalant aux automobilistes des dangers qui ne font pas courir de risque véritable aux conducteurs prudents. Imposer à la municipalité l'obligation d'installer un panneau dans un cas comme celui qui nous occupe équivaut à modifier la nature de l'obligation qu'ont les municipalités envers les conducteurs. Les municipalités ne sont pas tenues d'aménager des panneaux d'avertissement à l'intention des conducteurs en état d'ébriété et, ainsi, de remédier à leur incapacité de réagir aux indices qui alertent le conducteur moyen de la présence d'un danger.

Mes collègues affirment que la juge de première instance a dûment pris en considération tous les aspects du critère juridique applicable, y compris la question de savoir si la courbe présentait un risque pour le conducteur moyen qui prend des précautions normales. Ils disent que la juge de première instance a effectivement examiné, explicitement et implicitement, la conduite de l'automobiliste moyen ou raisonnable qui s'approche du virage. Ils font ensuite remarquer qu'elle a fait état du témoignage des experts MM. Anderson et Werner, qui ont tous deux analysé la conduite de l'automobiliste moyen se trouvant dans cette situation. Enfin, le fait qu'elle ait imputé une partie de la responsabilité à M. Nikolaisen indique, à leur avis, qu'elle a évalué sa conduite au regard à la norme du conducteur moyen, et qu'elle a donc pris en compte la façon dont ce dernier aurait conduit (par. 40).

I respectfully disagree that it is explicit in the trial judge's reasons that she considered whether the portion of the road on which the accident occurred posed a risk to the ordinary driver exercising reasonable care. As I explained above, the fact that the trial judge restated the legal test in the form of a conclusion in no way suggests that she turned her mind to the issue of whether the ordinary driver would have found the curve to be hazardous.

Nor do I agree that a discussion of the conduct of an ordinary motorist in the situation was somehow "implicit" in the trial judge's reasons. In my view, it is highly problematic to presume that a trial judge made factual findings on a particular issue in the absence of any indication in the reasons as to what those findings were. While a trial judge is presumed to know the law, he or she cannot be presumed to have reached a factual conclusion without some indication in the reasons that he or she did in fact come to that conclusion. If the reviewing court is willing to presume that a trial judge made certain findings based on evidence in the record absent any indication in the reasons that the trial judge actually made those findings, then the reviewing court is precluded from finding that the trial judge misapprehended or neglected evidence.

In my view, my colleagues have throughout their reasons improperly presumed that the trial judge reached certain factual findings based on the evidence despite the fact that those findings were not expressed in her reasons. On the issue of whether the curve presented a risk to the ordinary driver, my colleagues note that "in relying on the evidence of Mr. Anderson and Mr. Werner, the trial judge chose not to base her decision on the conflicting evidence of other witnesses" (para. 46). The problem with this statement is that although the trial judge relied on the evidence of Mr. Anderson and Mr. Werner to conclude that the portion of Snake Hill Road on which the accident occurred was a hazard, it is impossible from her reasons to discern what, if

137 En toute déférence, je ne crois pas qu'il ressorte explicitement des motifs de la juge de première instance qu'elle s'est demandé si la portion du chemin où s'est produit l'accident constituait un risque pour le conducteur raisonnable prenant des précautions normales. Comme je l'ai expliqué précédemment, le fait que la juge de première instance ait reformulé le critère juridique sous forme de conclusion n'indique aucunement qu'elle s'est demandé si le conducteur moyen aurait considéré la courbe comme dangereuse.

138 Je n'estime pas non plus que l'examen de la façon de conduire de l'automobiliste moyen dans cette situation ressorte « implicitement » des motifs de la juge de première instance. À mon avis, il est très problématique de présumer qu'un juge de première instance a tiré des conclusions de fait à l'égard d'une question précise alors qu'il n'y a aucune indication dans ses motifs quant à la nature de ces conclusions. Bien que le juge de première instance soit censé connaître le droit, on ne peut présumer qu'il a tiré à une conclusion factuelle en l'absence d'indication dans ses motifs qu'il est effectivement arrivé à cette conclusion. Si le tribunal de révision est prêt à supposer que le juge de première instance a tiré certaines conclusions, sur la foi de la preuve figurant au dossier, bien que rien dans les motifs n'indique qu'il a vraiment tiré ces conclusions, alors le tribunal de révision ne saurait conclure que le juge de première instance a mal interprété des éléments de preuve ou a négligé d'en tenir compte.

139 À mon avis, tout au long de leurs motifs, mes collègues ont à tort présumé que la juge de première instance était arrivée à certaines conclusions de fait fondées sur la preuve, malgré le fait que ces conclusions ne soient pas formulées dans ses motifs. Quant à la question de savoir si le virage présentait un risque pour le conducteur moyen, mes collègues ont fait remarquer qu'« en s'appuyant sur les témoignages de MM. Anderson et Werner, la juge de première instance a choisi de ne pas fonder sa décision sur les témoignages contradictoires rendus par d'autres témoins » (par. 46). Le problème que pose cet énoncé est que, même si la juge de première instance s'est appuyée sur les témoignages de MM. Anderson et Werner

any, evidence she relied on to reach the conclusion that the curve presented a risk to the ordinary driver exercising reasonable care. In the absence of any indication that she considered this issue, I am not willing to presume that she did.

140 My colleagues similarly presume findings of fact when discussing the knowledge of the municipality. On this issue, they reiterate that "it is open for a trial judge to prefer some parts of the evidence over others, and to re-assess the trial judge's weighing of the evidence, is, with respect, not within the province of an appellate court" (para. 62). At para. 64 of their reasons, my colleagues review the findings of the trial judge on the issue of knowledge and conclude that the trial judge "drew the inference that the municipality should have been put on notice and investigated Snake Hill Road, in which case it would have become aware of the hazard in question". I think that it is improper to conclude that the trial judge made a finding that the municipality's system of road inspection was inadequate in the absence of any indication in her reasons that she reached this conclusion. My colleagues further suggest that the trial judge did not impute knowledge to the municipality on the basis of the occurrence of prior accidents on Snake Hill Road (para. 65). They even state that it was not necessary for the trial judge to rely on the accidents in order to satisfy s. 192(3) (para. 67). This, in my view, is a reinterpretation of the trial judge's findings that stands in direct contradiction to the reasons that were provided by her. The trial judge discusses other factors pertaining to knowledge only to heighten the significance that she attributes to the fact that accidents had previously occurred on other portions of the road (at para. 90):

pour conclure que la portion du chemin Snake Hill où s'est produit l'accident constituait un danger, il est impossible, à partir de ses motifs, de dire si elle s'est appuyée sur un témoignage — et, dans l'affirmative, sur lequel de ceux-ci — pour conclure que la courbe présentait un risque pour le conducteur moyen qui prend des précautions raisonnables. En l'absence de toute indication que la juge de première instance s'est penchée sur cette question, je ne suis pas disposé à présumer qu'elle l'a fait.

De même, mes collègues supposent l'existence de conclusions factuelles dans leur examen de la question de la connaissance incombant à la municipalité. Sur ce point, ils réitèrent que « le juge de première instance peut préférer certaines parties de la preuve à d'autres, et, en toute déférence, il n'appartient pas au tribunal d'appel de procéder à nouveau à l'appréciation de la preuve, tâche déjà accomplie par le juge de procès » (par. 62). Au paragraphe 64 de leurs motifs, mes collègues examinent les conclusions de la juge de première instance sur la question de la connaissance et concluent qu'elle « a inféré que la municipalité aurait dû être informée de la situation sur le chemin à Snake Hill et aurait dû faire enquête à cet égard, ce qui lui aurait permis de prendre connaissance de l'existence du danger ». Je ne crois pas qu'on puisse à juste titre conclure que la juge de première instance est arrivée à la conclusion que le système d'inspection routière de la municipalité était inadéquat, alors que rien dans ses motifs n'indique qu'elle a tiré cette conclusion. Mes collègues estiment en outre que la juge de première instance n'a pas prêté à la municipalité la connaissance requise sur la base des accidents survenus antérieurement sur le chemin Snake Hill (par. 65). Ils disent même qu'il n'était pas nécessaire de s'appuyer sur ces accidents pour satisfaire aux exigences du par. 192(3) (par. 67). À mon avis, ils donnent à ces conclusions une nouvelle interprétation, qui contredit directement les motifs qu'elle a exposés. La juge de première instance examine d'autres facteurs qui touchent à la connaissance requise, uniquement pour souligner l'importance qu'elle accorde au fait que des accidents sont survenus antérieurement ailleurs sur le chemin (au par. 90) :

If the R.M. did not have actual knowledge of the danger inherent in this portion of Snake Hill Road, it should have known. While four accidents in 12 years may not in itself be significant, it takes on more significance given the close proximity of three of these accidents, the relatively low volume of traffic, the fact that there are permanent residences on the road and the fact that the road is frequented by young and perhaps less experienced drivers. [Emphasis added.]

My colleagues refer to the decision of *Van de Perre v. Edwards*, [2001] 2 S.C.R. 1014, 2001 SCC 60, in which I stated that "an omission [in the trial judge's reasons] is only a material error if it gives rise to the reasoned belief that the trial judge must have forgotten, ignored or misconceived the evidence in a way that affected his conclusion" (para. 15). This case is however distinguishable from *Van de Perre*. In *Van de Perre*, the appellate court improperly substituted its own findings of fact for the trial judge's clear factual conclusions on the basis that the trial judge had not considered all of the evidence. By contrast, in this case my colleagues assert that this Court should not interfere with the "findings of the trial judge" even where no findings were made and where such findings must be presumed from the evidence. The trial judge's failure in this case to reach any conclusion on whether the ordinary driver would have found the portion of the road on which the accident occurred hazardous, in my view, gives rise to the reasoned belief that she ignored the evidence on the issue in a way that affected her conclusion.

Finally, I do not agree that the trial judge's conclusion that Mr. Nikolaisen was negligent equates to an assessment of whether a motorist exercising ordinary care would have found the curve on which the accident occurred to be hazardous. It is clear from the trial judge's reasons that she made a factual finding that the curve could be driven safely at 60 km/h in dry conditions and 50 km/h in wet conditions and that Mr. Nikolaisen approached the curve at an

[TRADUCTION] Si la M.R. ne connaissait pas concrètement le danger intrinsèque que comporte cette portion du chemin Snake Hill, elle aurait dû le connaître. Le fait que quatre accidents se soient produits en 12 ans n'est peut-être pas significatif en soi, mais il le devient si l'on considère que trois de ces accidents sont survenus à proximité, qu'il s'agit d'une route à débit de circulation relativement faible, que des résidences permanentes sont situées en bordure de celle-ci et que ce chemin est fréquenté par des conducteurs jeunes et peut-être moins expérimentés. [Je souligne.]

141 Mes collègues citent l'arrêt *Van de Perre c. Edwards*, [2001] 2 R.C.S. 1014, 2001 CSC 60, dans lequel j'ai dit, au par. 15, qu'« une omission [dans les motifs du juge de première instance] ne constitue une erreur importante que si elle donne lieu à la conviction rationnelle que le juge de première instance doit avoir oublié, négligé d'examiner ou mal interprété la preuve de telle manière que sa conclusion en a été affectée ». Cependant, le présent pourvoi peut être distingué de l'affaire *Van de Perre*. Dans cette affaire, la Cour d'appel avait irrégulièrement substitué ses propres conclusions de fait aux conclusions factuelles évidentes du juge de première instance, au motif que celui-ci n'avait pas pris en compte tous les éléments de preuve. Par contraste, dans le présent pourvoi, mes collègues affirment que notre Cour ne doit pas modifier les « conclusions de la juge de première instance », même si aucune conclusion n'a été tirée et s'il faut supposer leur existence à partir de la preuve. En l'espèce, je suis d'avis que l'omission de la juge de première instance de tirer quelque conclusion que ce soit quant à la question de savoir si le conducteur moyen aurait considéré comme dangereux le tronçon du chemin où s'est produit l'accident fait naître la conviction rationnelle que, sur ce point, elle a négligé d'examiner la preuve de telle manière que sa conclusion en a été affectée.

142 Enfin, je ne peux souscrire à l'opinion que la conclusion de la juge de première instance selon laquelle M. Nikolaisen a fait preuve de négligence vaut examen de la question de savoir si l'automobiliste moyen prenant des précautions normales aurait estimé que la courbe où s'est produit l'accident était dangereuse. Il ressort clairement des motifs de la juge de première instance qu'elle a tiré les conclusions de fait suivantes : il était possible de prendre

excessive speed. As earlier stated, what she failed to consider was whether the ordinary driver exercising reasonable care would have approached the curve at a speed at which it could be safely negotiated, or, stated differently, whether the curve posed a real danger to the ordinary driver.

B. *Did the Trial Judge Err in Finding that the Respondent Municipality Knew or Should Have Known of the Danger Posed by the Municipal Road?*

143 Pursuant to s. 192(3) of *The Rural Municipality Act, 1989*, fault is not to be imputed to the municipality in the absence of proof by the plaintiff that the municipality "knew or should have known of the disrepair".

144 The trial judge made no finding that the respondent municipality had actual knowledge of the alleged state of disrepair, but rather imputed knowledge to the respondent on the basis that it should have known of the danger. This is apparent in her findings on knowledge at paras. 89-91 of her reasons:

> Breach of the statutory duty of care imposed by section 192 of the *Rural Municipality Act*, *supra*, cannot be imputed to the R.M. unless it knew of or ought to have known of the state of disrepair on Snake Hill Road. Between 1978 and 1990 there were four accidents on Snake Hill Road. Three of these accidents occurred in the same vicinity as the Nikolaisen rollover. The precise location of the fourth accident is unknown. While at least three of these accidents occurred when motorists where travelling in the opposite direction of the Nikolaisen vehicle, they occurred on that portion of Snake Hill Road which is the most dangerous — where the road begins to curve, rather than where it is generally straight and flat. At least two of these accidents were reported to authorities.
>
> If the R.M. did not have actual knowledge of the danger inherent in this portion of Snake Hill Road, it should have known. While four accidents in 12 years may not in itself be significant, it takes on more significance

le virage en sécurité à 60 km/h à l'heure sur chaussée sèche et à 50 km/h sur chaussée humide, et M. Nikolaisen s'est approché du virage à une vitesse excessive. Comme je l'ai indiqué plus tôt, elle a omis de se demander si le conducteur moyen qui prend des précautions normales se serait approché du virage à une vitesse qui lui aurait permis de le prendre en sécurité ou, autrement dit, si la courbe présentait un danger réel pour le conducteur moyen.

B. *La juge de première instance a-t-elle commis une erreur en concluant que la municipalité intimée connaissait ou aurait dû connaître le danger que présentait le chemin municipal?*

Conformément au par. 192(3) de la *Rural Municipality Act, 1989*, aucune faute n'est imputée à la municipalité à moins que le demandeur n'établisse que celle-ci « connaissait ou aurait dû connaître le mauvais état du chemin ».

La juge de première instance n'a pas conclu que la municipalité intimée connaissait concrètement le mauvais état dans lequel se trouvait, prétend-on, le chemin, mais elle lui a plutôt prêté cette connaissance pour le motif qu'elle aurait dû connaître l'existence du danger. C'est ce qui ressort de ses conclusions à cet égard, aux par. 89 à 91 de ses motifs :

> [TRADUCTION] On ne peut reprocher à la municipalité rurale d'avoir manqué à l'obligation légale de diligence imposée par l'art. 192 de la loi intitulée la *Rural Municipality Act*, précitée, que si la municipalité connaissait ou aurait dû connaître le mauvais état du chemin Snake Hill. De 1978 à 1990, quatre accidents sont survenus sur ce chemin. Trois de ces accidents ont eu lieu dans le même secteur que celui où le véhicule de Nikolaisen a fait un tonneau. On ne connaît pas le lieu précis du quatrième accident. Bien que, dans au moins trois de ces accidents, les automobilistes aient circulé en sens inverse du véhicule de Nikolaisen, les accidents se sont produits dans la partie la plus dangereuse du chemin Snake Hill — là où commencent les courbes, et non dans la partie où le chemin est généralement droit et plat. Au moins deux de ces accidents ont été signalés aux autorités.
>
> Si la M.R. ne connaissait pas concrètement le danger intrinsèque que comporte cette portion du chemin Snake Hill, elle aurait dû le connaître. Le fait que quatre accidents se soient produits en 12 ans n'est peut-être pas

given the close proximity of three of these accidents, the relatively low volume of traffic, the fact that there are permanent residences on the road and the fact that the road is frequented by young and perhaps less experienced drivers. I am not satisfied that the R.M. has established that in these circumstances it took reasonable steps to prevent this state of disrepair on Snake Hill Road from continuing.

I find that by failing to erect and maintain a warning and regulatory sign on this portion of Snake Hill Road the R.M. has not met the standard of care which is reasonable in the circumstances. Accordingly, it is in breach of its duty of care to motorists generally, and to Mr. Housen in particular. [Emphasis added.]

Whether the municipality should have known of the disrepair (here, the risk posed in the absence of a sign) involves both questions of law and questions of fact. As a matter of law, the trial judge must approach the question of whether knowledge should be imputed to the municipality with regard to the duties of the ordinary, reasonable and prudent municipal councillor (*Ryan v. Victoria (City)*, [1999] 1 S.C.R. 201, at para. 28). The question is then answered through the trial judge's assessment of the facts of the case.

I find that the trial judge made both errors of law and palpable and overriding errors of fact in determining that the respondent municipality should have known of the alleged state of disrepair. She erred in law by approaching the question of knowledge from the perspective of an expert rather than from the perspective of a prudent municipal councillor. She also erred in law by failing to appreciate that the onus of proving that the municipality knew or should have known of the alleged disrepair remained on the plaintiff throughout. The trial judge clearly erred in fact by drawing the unreasonable inference that the respondent municipality should have known that the portion of the road on which the accident occurred was dangerous from evidence that accidents had occurred on other parts of Snake Hill Road.

significatif en soi, mais il le devient si l'on considère que trois de ces accidents sont survenus à proximité, qu'il s'agit d'une route à débit de circulation relativement faible, que des résidences permanentes sont situées en bordure de celle-ci et que le chemin est fréquenté par des conducteurs jeunes et peut-être moins expérimentés. Je ne suis pas convaincue que la M.R. a établi avoir, dans ces circonstances, pris des mesures raisonnables pour remédier au mauvais état du chemin Snake Hill.

J'estime que, en omettant d'installer et de maintenir un panneau d'avertissement ou de signalisation dans cette partie du chemin Snake Hill, la M.R. n'a pas satisfait à la norme de diligence qui est raisonnable dans les circonstances. Par conséquent, elle ne s'est pas acquittée de son obligation de diligence à l'égard des automobilistes en général et à l'égard de M. Housen en particulier. [Je souligne.]

145 La question de savoir si la municipalité aurait dû connaître le mauvais état du chemin (en l'occurrence, le risque que présentait l'absence de signalisation) soulève à la fois des questions de droit et des questions de fait. Sur le plan juridique, le juge de première instance doit se demander s'il y a lieu de présumer que la municipalité connaissait ce fait, au regard des obligations qui incombent au conseiller municipal ordinaire, raisonnable et prudent (*Ryan c. Victoria (Ville)*, [1999] 1 R.C.S. 201, par. 28). Le juge de première instance répond ensuite à la question en appréciant les faits de l'espèce dont il est saisi.

146 J'estime que la juge de première instance a commis et des erreurs de droit et des erreurs de fait manifestes et dominantes en statuant que la municipalité intimée aurait dû connaître le mauvais état dans lequel se trouvait, prétend-on, le chemin. Elle a commis une erreur de droit lorsqu'elle a examiné la question de la connaissance du point de vue du spécialiste plutôt que du point de vue du conseiller municipal prudent. Elle a commis une autre erreur de droit en ne reconnaissant pas que le fardeau de prouver que la municipalité connaissait ou aurait dû connaître le mauvais état du chemin ne cessait jamais d'incomber au demandeur. La juge de première instance a clairement commis une erreur de fait en inférant déraisonnablement que la municipalité intimée aurait dû savoir que la partie du chemin où l'accident s'est produit était dangereuse, compte tenu de la preuve que des accidents avaient eu lieu ailleurs sur le chemin Snake Hill.

147 The trial judge's failure to determine whether knowledge should be imputed to the municipality from the perspective of what a prudent municipal councillor should have known is implicit in her reasons. The respondent could not be held, for the purposes of establishing knowledge under the statutory test, to the standard of an expert analysing the curve after the accident. Yet this is precisely what the trial judge did. She relied on the expert evidence of Mr. Anderson and Mr. Werner to reach the conclusion that the curve presented a hidden hazard. She also implicitly accepted that the risk posed by the curve was not one that would be readily apparent to a lay person. This is evident in the portion of her judgment where she accepts as a valid excuse for not filing a timely claim against the respondent the appellant counsel's explanation that he did not believe the respondent to be at fault until expert opinions were obtained. The trial judge stated in this regard: "[i]t was only later when expert opinions were obtained that serious consideration was given to the prospect that the nature of Snake Hill Road might be a factor contributing to the accident" (para. 64). Her failure to consider the risk to the prudent driver is also apparent when one considers that she ignored the evidence concerning the way in which the two experts themselves had approached the dangerous curve (see para. 54 above).

Il ressort implicitement des motifs de la juge de première instance qu'elle n'a pas décidé s'il fallait prêter à la municipalité la connaissance requise en considérant cette question du point de vue du conseiller municipal prudent. Pour trancher la question de la connaissance requise suivant le critère prévu par la loi, l'intimée ne pouvait être tenue aux mêmes normes qu'un spécialiste analysant la courbe après l'accident. Pourtant, c'est exactement ce qu'a fait la juge de première instance. Elle s'est fondée sur les témoignages d'expert donnés par MM. Anderson et Werner pour conclure que la courbe présentait un danger caché. Elle a également reconnu implicitement que le risque visé par la courbe n'était pas un risque facilement décelable par un profane. Cela ressort clairement du passage de son jugement où elle considère comme une excuse valable pour justifier le dépôt tardif de l'action contre l'intimée l'explication de l'avocat de l'appelant selon laquelle il ne croyait pas que l'intimée était dans son tort jusqu'à ce qu'il prenne connaissance des opinions des experts. La juge de première instance a dit ceci à cet égard : [TRADUCTION] « [c]e n'est que plus tard, après avoir obtenu l'opinion des experts, que la possibilité que la nature du chemin Snake Hill puisse avoir été un facteur ayant contribué à l'accident a été sérieusement envisagée » (par. 64). Son omission de s'interroger sur le risque que courrait le conducteur prudent apparaît elle aussi clairement, lorsqu'on considère qu'elle n'a pas tenu compte de la preuve concernant la façon dont les deux experts avaient eux-mêmes pris le virage dangereux (voir le par. 54 qui précède).

148 Had the trial judge considered the question of whether the municipality should have known of the alleged disrepair from the perspective of the prudent municipal councillor, she would necessarily have reached a different conclusion. There was no evidence that the road conditions which existed posed a risk that the respondent should have been aware of. The respondent had no particular reason to inspect that segment of the road for the presence of hazards. It had not received any complaints from motorists respecting the absence of signs on the road, the lack of superelevation on the curves, or the presence of

Si la juge de première instance avait répondu à la question de savoir si la municipalité aurait dû connaître le mauvais état dans lequel se trouvait, prétend-on, le chemin en se plaçant du point de vue du conseiller municipal prudent, elle serait nécessairement arrivée à une conclusion différente. Il n'y avait aucune preuve établissant que le danger existant créait un risque que l'intimée aurait dû connaître. Cette dernière n'avait aucune raison particulière d'aller inspecter cette portion du chemin pour voir s'il y existait des dangers. Elle n'avait reçu aucune plainte d'automobilistes relativement à l'absence de signalisation, à l'absence de surélévation des

trees and vegetation which grew up along the sides of the road.

In addition, the question of the respondent's knowledge is linked inextricably to the standard of care. A municipality can only be expected to have knowledge of those hazards which pose a risk to the reasonable driver exercising ordinary care, since these are the only hazards for which there is a duty to repair. The trial judge should not have expected the respondent in this case to have knowledge of the road conditions that existed at the site of the Nikolaisen rollover since that road condition simply did not pose a risk to the reasonable driver. In addition to the evidence that was discussed above in the context of the standard of care, this conclusion is supported by the testimony of the several lay witnesses that testified at trial. Craig Thiel, a resident on the road, testified that he was not aware that Snake Hill Road had a reputation of being a dangerous road, and that he himself had never experienced difficulty with the portion of the road on which the accident occurred. His wife, Toby, also testified that she had experienced no problems with the road.

The trial judge also clearly erred in fact by imputing knowledge to the municipality on the basis of the four accidents that had previously occurred on Snake Hill Road. While her factual findings regarding the accidents themselves have a sound basis in the evidence, these findings simply do not support her conclusion that a prudent municipal councillor ought to have known that a risk existed for the normal prudent driver. As such, the trial judge erred in drawing an unreasonable inference from the evidence that was before her. As stated above, the standard of review for inferences of fact is, above all, one of reasonableness. This is reflected in the following passage from *Joseph Brant Memorial Hospital v. Koziol*, [1978] 1 S.C.R. 491, at pp. 503-4:

. . . "it is a well-known principle that appellate tribunals should not disturb findings of fact made by a trial judge

courbes ou à la présence d'arbres et de végétation en bordure du chemin.

149 En outre, la question de la connaissance de l'intimée est intimement liée à celle de la norme de diligence. Une municipalité est uniquement censée avoir connaissance des dangers qui présentent un risque pour le conducteur raisonnable prenant des précautions normales, puisqu'il s'agit des seuls dangers à l'égard desquels existe une obligation d'entretien. En l'espèce, la juge de première instance n'aurait pas dû attendre de l'intimée qu'elle connaisse le danger qui existait à l'endroit où le véhicule de M. Nikolaisen a fait un tonneau, puisque ce danger ne présentait tout simplement pas de risque pour le conducteur raisonnable. Outre les éléments de preuve examinés précédemment relativement à la norme de diligence, les témoignages de plusieurs témoins ordinaires qui ont déposé au procès étayent cette conclusion. Craig Thiel, qui habite le long de ce chemin, a témoigné qu'il ne savait pas que le chemin Snake Hill avait la réputation d'être dangereux et qu'il n'avait lui-même jamais éprouvé de difficulté à conduire à l'endroit du chemin où est survenu l'accident. Sa conjointe, Toby, a également dit ne pas avoir connu de problème sur ce chemin.

150 La juge de première instance a clairement commis une autre erreur de fait en présumant, sur la foi des quatre accidents survenus auparavant sur le chemin Snake Hill, que la municipalité connaissait l'existence du danger. Bien que ses conclusions de fait relativement aux accidents eux-mêmes soient solidement étayées par la preuve, elles n'appuient tout simplement pas sa conclusion qu'un conseiller municipal prudent aurait dû savoir qu'il existait un risque pour le conducteur prudent. En conséquence, la juge de première instance a fait erreur en tirant une inférence déraisonnable de la preuve qui lui était soumise. Comme il a été indiqué plus tôt, la norme de contrôle applicable aux inférences de fait est, d'abord et avant tout, celle de la décision raisonnable. Les propos suivants du juge Spence dans l'arrêt *Joseph Brant Memorial Hospital c. Koziol*, [1978] 1 R.C.S. 491, p. 503-504, illustrent bien ce principe :

. . . « c'est un principe bien connu que les tribunaux d'appel ne doivent pas remettre en cause les conclusions

if there were credible evidence before him upon which he could reasonably base his conclusion". [Emphasis added.]

151 As I stated above, there was no evidence to suggest that the respondent had actual knowledge that accidents had previously occurred on Snake Hill Road. To the contrary, Mr. Danger, the administrator of the municipality, testified that the first he heard of the accidents was at the trial.

152 Implicit in the trial judge's reasons, then, was the expectation that the municipality should have known about the accidents through an accident-reporting system**.** The appellant put forward that argument explicitly before this Court, placing significant emphasis on the fact that respondent "has no regularized approach to gathering this information, whether from councillors or otherwise". The argument suggests that, had the municipality established a formal system to find out whether accidents had occurred on a given road, it would have known that accidents had occurred on Snake Hill Road and would have taken the appropriate corrective action to ensure that the road was safe for travellers.

153 I find the above argument to be flawed in two important respects. First, the argument that the other accidents on Snake Hill Road were relevant in this case is based on the assumption that there was an obligation on the respondent municipality to have a "regularized" accident-reporting system, and that the informal system that was in place was somehow deficient. In my view, the appellant did not meet its onus to show that the system relied on by the municipality to discharge its obligations under s. 192 of the *The Rural Municipality Act, 1989* was deficient. The evidence shows that, prior to 1988, there was no formal system of accident reporting in place. There was, nonetheless, an informal system whereby the municipal councillors were responsible for finding out if there were road hazards. Information that hazards existed came to the attention of the councillors via complaints, and from their own familiarity

de fait du juge de première instance, s'il existait des témoignages dignes de foi sur lesquels le juge pouvait raisonnablement fonder ses conclusions ». [Je souligne.]

Comme je l'ai mentionné précédemment, il n'y avait aucune preuve indiquant que l'intimée savait concrètement que d'autres accidents étaient survenus auparavant sur le chemin Snake Hill. Au contraire, M. Danger, l'administrateur de la municipalité, a témoigné qu'il avait entendu parler de ces accidents pour la première fois au procès.

Par conséquent, il ressort implicitement des motifs de la juge de première instance que la municipalité aurait censément dû connaître l'existence des accidents grâce à un système d'information en la matière. L'appelant a expressément plaidé cet argument devant notre Cour, insistant fortement sur le fait que l'intimée [TRADUCTION] « ne dispose pas d'un mécanisme structuré de collecte de cette information, que ce soit par l'entremise des conseillers ou d'autres personnes ». Suivant cet argument, on prétend que, si la municipalité avait établi un système officiel lui permettant de savoir si des accidents sont survenus sur une route donnée, elle aurait su que des accidents s'étaient produits sur le chemin Snake Hill et elle aurait pris les mesures correctives appropriées pour faire en sorte que le chemin soit sécuritaire pour les usagers.

J'estime que l'argument susmentionné présente deux lacunes importantes. Premièrement, l'argument selon lequel les autres accidents survenus sur le chemin Snake Hill étaient pertinents en l'espèce repose sur la présomption que la municipalité intimée avait l'obligation d'avoir un système « structuré » d'information sur les accidents, et que le système informel en place était d'une certaine manière déficient. À mon avis, l'appelant ne s'est pas acquitté du fardeau qui lui incombait de démontrer que le système sur lequel la municipalité se fondait pour remplir ses obligations au titre de l'art. 192 de la *Rural Municipality Act, 1989*, était déficient. La preuve établit que, avant 1988, il n'existait pas de système officiel d'information sur les accidents. Il existait néanmoins, un système informel dans le cadre duquel les conseillers municipaux étaient chargés de s'enquérir de l'existence de dangers

with the roads within the township under their jurisdiction. The trial judge made a palpable error in finding that this informal system was deficient in the absence of any evidence of the practice of other municipalities at the time that the accidents occurred and what might have been a reasonable system, particularly given the fact that the rural municipality in question had only six councillors. There is no evidence that a rural municipality of this type requires the sort of sophisticated information-gathering process that may be required in a city, where accidents occur with greater frequency and where it is less likely that word of mouth will suffice to bring hazards to the attention of the councillors.

sur les routes. Les conseillers étaient informés de l'existence de dangers par suite des plaintes qu'ils recevaient et par leur propre expérience des routes situées dans les cantons qu'ils représentaient. La juge de première instance a commis une erreur manifeste en concluant que ce système informel était déficient, alors qu'aucune preuve n'indiquait quelles étaient les pratiques suivies par d'autres municipalités à cet égard au moment des accidents, ni n'expliquait en quoi aurait consisté un système raisonnable, compte tenu particulièrement du fait que la municipalité rurale concernée ne comptait que six conseillers. Il n'y a aucune preuve indiquant qu'une municipalité rurale de ce genre a besoin du genre de mécanisme élaboré de collecte de renseignements dont peut avoir besoin une grande ville, où les accidents sont plus fréquents et où il est peu probable que le bouche à oreille soit suffisant pour porter les dangers à l'attention des conseillers.

The respondent municipality now has a more formalized system of accident reporting. Since 1988, Saskatchewan Highways and Transportation annually provides the municipalities with a listing of all motor vehicle accidents which occur within the municipality and which are reported to the police. While I agree that this system may provide the municipality with a better chance of locating hazards in some circumstances, I do not accept that the adoption of this system is relevant on the facts of this case. Only one accident, which occurred in 1990, was reported to the respondent under this system. The appellant adduced no evidence to suggest that this accident occurred at the same location as the Nikolaisen rollover, or that this accident occurred as a result of the conditions of the road rather than the negligence of the driver.

154 La municipalité intimée possède maintenant un système plus officiel d'information sur les accidents. Depuis 1988, en effet, le ministère de la Voirie et du Transport de la Saskatchewan communique annuellement à chaque municipalité la liste de tous les accidents d'automobile survenus sur son territoire et signalés aux policiers. Bien que ce système puisse, j'en conviens, permettre aux municipalités de mieux repérer les dangers dans certaines circonstances, je ne crois pas que son adoption soit pertinente eu égard aux faits de l'espèce. Un seul accident, survenu en 1990, a été signalé à l'intimée par le truchement de ce système. L'appelant n'a produit aucun élément de preuve indiquant que cet accident est survenu au même endroit que celui où le véhicule de M. Nikolaisen a fait un tonneau, ou qu'il était attribuable à l'état de la route plutôt qu'à la négligence du conducteur.

Secondly, and perhaps more importantly, it was simply illogical for the trial judge to infer from the fact of the earlier accidents that the respondent should have known that the site of the Nikolaisen rollover posed a risk to prudent drivers. The three accidents, which took place in 1978, 1985, and 1987, occurred on different curves, while the vehicles involved were proceeding in the opposite

155 Deuxièmement, élément peut-être plus important encore, il était tout simplement illogique pour la juge de première instance d'inférer de l'existence des accidents antérieurs que l'intimée aurait dû savoir que l'endroit où le véhicule de M. Nikolaisen a fait un tonneau présentait un risque pour les conducteurs prudents. Les trois accidents — qui sont survenus en 1978, 1985 et 1987

direction. The accidents of 1978 and 1987 occurred on the first right-turning curve in the road with the drivers travelling westbound, at the bottom of the hill. The accident in 1985 took place on the next curve in the road with the driver also travelling westbound, again on a different curve from the one where the Nikolaisen rollover took place. If anything, these accidents signal that the municipality should have been concerned with the curves that were, when travelling westbound, to the east of the site of the Nikolaisen rollover. The evidence disclosed no accidents that had occurred at the precise location of the accident that is the subject of this case.

— se sont produits dans des courbes différentes, et les véhicules concernés circulaient en sens inverse. L'accident de 1978 et celui de 1987 ont eu lieu dans le premier virage à droite au pied de la colline, les automobilistes roulant alors en direction ouest. L'accident de 1985 s'est produit dans la deuxième courbe, toujours en direction ouest, encore une fois dans une courbe différente de celle où le véhicule de M. Nikolaisen a fait un tonneau. Si ces accidents indiquent quoi que ce soit, c'est plutôt que la municipalité aurait dû se préoccuper des courbes qui, pour les véhicules circulant en direction ouest, se trouvent à l'est de l'endroit où le véhicule de M. Nikolaisen a fait un tonneau. La preuve n'a révélé aucun accident qui se serait produit à l'endroit précis où est survenu l'accident qui nous intéresse.

156 Furthermore, the mere occurrence of an accident does not in and of itself indicate a duty to post a sign. In many cases, accidents happen not because of the conditions of the road, but rather because of the negligence of the driver. Illustrative in this regard is Mr. Agrey's accident on Snake Hill Road in 1978. Mr. Agrey testified that, just prior to the accident, he had turned his attention away from the road to talk to one of the passengers in the vehicle. Another passenger shouted to him to "look out", but by the time he was alerted it was too late to properly navigate the turn. Mr. Agrey was charged and fined for his carelessness. As was discussed in the context of the standard of care, a municipality is not obligated to make safe the roads for all drivers, regardless of the care and attention that they are exercising when driving. It need only keep roads in such a state of repair as will allow a reasonable driver exercising ordinary care to drive with safety.

Qui plus est, le simple fait qu'un accident se produise n'emporte pas en soi l'obligation d'installer un panneau signalisateur. Dans bien des cas, les accidents surviennent non pas à cause de l'état de la route, mais plutôt à cause de la négligence du conducteur. Un bon exemple de cela est l'accident dont a été victime M. Agrey sur le chemin Snake Hill en 1978. Ce dernier a témoigné que, juste avant l'accident, il avait quitté des yeux la route pour parler à l'un des passagers du véhicule. Un autre passager lui a crié de faire attention, mais il était déjà trop tard pour bien exécuter le virage. Accusé de conduite imprudente, M. Agrey a été déclaré coupable et condamné à une amende. Comme on l'a vu plus tôt, dans le contexte de la norme de diligence, une municipalité n'a pas l'obligation de rendre les chemins sécuritaires pour tous les conducteurs, indépendamment de la prudence et de l'attention avec lesquelles ils conduisent. Elle est seulement tenue de maintenir les chemins dans un état propre à permettre au conducteur raisonnable qui prend des précautions normales d'y circuler en sécurité.

157 In addition to the substantial errors discussed above, I would also note that, in my view, the trial judge was inattentive to the onus of proof on this issue. When reviewing the evidence pertaining to other accidents on Snake Hill Road, the trial judge remarked, at para. 31: "Cst. Forbes does not recall

Outre les erreurs substantielles examinées précédemment, je tiens également à souligner que, selon moi, la juge de première instance ne s'est pas souciée du fardeau de preuve sur cette question. Lorsqu'elle a examiné la preuve relative aux autres accidents survenus sur le chemin Snake Hill, la juge

any other accident on Snake Hill Road during her time at the Shellbrook RCMP Detachment, from 1987 until 1996. Cpl. Healey had heard of one other accident. Forbes and Healey are only two of nine members of the RCMP Detachment at Shellbrook" (emphasis added). By this comment, the trial judge seems to imply that there may have been more accidents on Snake Hill Road that had been reported and that the respondent should have known about this. With all due respect to the trial judge, if there had been accidents other than the ones that were raised at trial, it was up to the appellant to bring evidence of these accidents forward, either by calling the RCMP members to whom they had been reported, or by calling those who were involved in the accidents, or by any other available means. Furthermore, the significance that the trial judge attributed to the other accidents that occurred on Snake Hill Road was dependent on her assumption that the respondent should have had a formal accident-reporting system in place. The respondent did not bear the onus of demonstrating that it was not obliged to have such a system; there was, rather, a positive onus on the appellant to demonstrate that such a system was required and that the informal reporting system was inadequate.

C. *Did the Trial Judge Err in Finding that the Accident was Caused in Part by the Failure of the Respondent Municipality to Erect a Sign Near the Curve?*

The trial judge's findings on causation are found at para. 101 of her judgment, where she states:

I find that this accident occurred as a result of Mr. Nikolaisen entering the curve on Snake Hill Road at a speed slightly in excess of that which would allow successful negotiation. The accident occurred at the most dangerous segment of Snake Hill Road where a warning or regulatory sign should have been erected and maintained to warn motorists of an impending and hidden hazard. Mr. Nikolaisen's degree of impairment only

de première instance a fait les remarques suivantes au par. 31 : [TRADUCTION] « La gendarme Forbes ne se souvient pas de quelque autre accident sur le chemin Snake Hill durant la période où elle était affectée au détachement de la GRC de Shellbrook, de 1987 à 1996. Le caporal Healey avait entendu parler d'un autre accident. Forbes et Healey ne sont que deux des neuf membres du détachement de la GRC à Shellbrook » (je souligne). Par cette remarque, la juge de première instance semble laisser entendre que d'autres accidents sur le chemin Snake Hill ont pu avoir été signalés et que l'intimée aurait dû le savoir. En toute déférence pour la juge de première instance, s'il y avait eu d'autres accidents que ceux qui ont été mentionnés au procès, il appartenait à l'appelant d'en faire la preuve, soit en faisant témoigner les membres de la GRC à qui les accidents avaient été signalés ou encore les personnes en cause dans ces accidents, soit en utilisant tout autre moyen à sa disposition. En outre, l'importance que la juge de première instance a accordée aux autres accidents survenus sur le chemin Snake Hill dépendait du postulat que l'intimée aurait dû posséder un système officiel d'information sur les accidents. L'intimée n'était pas tenue de prouver qu'elle n'avait pas l'obligation de disposer d'un tel système. Il incombait plutôt à l'appelant d'établir que ce genre de système était nécessaire et que le système informel existant était insuffisant.

C. *La juge de première instance a-t-elle commis une erreur en concluant que l'accident avait été causé, en partie, par le défaut de la municipalité intimée d'installer un panneau de signalisation près de la courbe?*

158 Les conclusions de la juge de première instance au sujet du lien de causalité figurent au par. 101 de son jugement, où elle dit ceci :

[TRADUCTION] J'estime que l'accident s'est produit parce que M. Nikolaisen s'est engagé dans le virage sur le chemin Snake Hill à une vitesse légèrement supérieure à celle qui lui aurait permis de réussir la manœuvre. L'accident est survenu dans la portion la plus dangereuse du chemin Snake Hill, à un endroit où un panneau d'avertissement ou de signalisation aurait dû être installé et maintenu pour avertir les automobilistes de

served to increase the risk of him not reacting, or reacting inappropriately to a sign. Mr. Nikolaisen was not driving recklessly such that he would have intentionally disregarded a warning or regulatory sign. He had moments earlier, when departing the Thiel residence, successfully negotiated a sharp curve which he could see and which was apparent to him. I am satisfied on a balance of probabilities that had Mr. Nikolaisen been forewarned of the curve, he would have reacted and taken appropriate corrective action such that he would not have lost control of his vehicle when entering the curve.

159 The trial judge's above findings in respect to causation represent conclusions on matters of fact. Consequently, this Court will only interfere if it finds that in coming to these conclusions she made a manifest error, ignored conclusive or relevant evidence, misunderstood the evidence, or drew erroneous conclusions from it (*Toneguzzo-Norvell*, *supra*, at p. 121).

160 In coming to her conclusion on causation, the trial judge made several of the types of errors that this Court referred to in *Toneguzzo-Norvell*. To the extent that the trial judge relied on the evidence of Mr. Laughlin, the only expert to have testified on the issue of causation, I find that she either misunderstood his evidence or drew erroneous conclusions from it. The only other testimony in respect to causation was anecdotal evidence pertaining to Mr. Nikolaisen's level of impairment provided by Craig Thiel, Toby Thiel and Paul Housen. Although their testimonies provided some evidence in respect to causation, for reasons I will discuss, it was not evidence on which the trial judge could reasonably rely. Nor do I find that the trial judge was entitled to rely on evidence that Mr. Nikolaisen successfully negotiated the curve from the Thiel driveway onto Snake Hill Road. The inference that the trial judge drew from this fact was unreasonable and ignored evidence that Mr. Nikolaisen swerved even on this curve. In addition, the trial judge clearly erred by ignoring other relevant evidence in respect to causation, in particular the fact that Mr. Nikolaisen had driven on the

l'imminence d'un danger caché. Le degré d'ébriété de M. Nikolaisen n'a fait qu'accroître le risque qu'il ne réagisse pas du tout ou encore de façon inappropriée à une signalisation. M. Nikolaisen ne conduisait pas de façon si téméraire qu'il aurait intentionnellement fait abstraction d'un panneau d'avertissement ou de signalisation. Quelques instants plus tôt, au moment de quitter la résidence des Thiel, il avait pris avec succès un virage serré qu'il pouvait clairement voir. Je suis convaincue, selon la prépondérance des probabilités, que si on avait prévenu M. Nikolaisen de l'existence de la courbe, il aurait réagi et pris des mesures appropriées, qui l'auraient empêché de perdre la maîtrise de son véhicule en s'engageant dans le virage.

Les conclusions susmentionnées de la juge de première instance touchant le lien de causalité sont des conclusions portant sur des questions de fait. Par conséquent, notre Cour n'interviendra que si elle estime que, pour arriver à ses conclusions, la juge a commis une erreur manifeste, n'a pas tenu compte d'un élément de preuve déterminant ou pertinent, a mal compris la preuve ou en a tiré des conclusions erronées (*Toneguzzo-Norvell*, précité, p. 121).

En arrivant à sa conclusion sur le lien de causalité, la juge de première instance a commis plusieurs des erreurs mentionnées par notre Cour dans l'arrêt *Toneguzzo-Norvell*, précité. Dans la mesure où la juge de première instance s'est fondée sur le témoignage de M. Laughlin, le seul expert à avoir témoigné sur la question du lien de causalité, j'estime qu'elle a mal interprété son témoignage ou qu'elle en a tiré des conclusions erronées. Les éléments anecdotiques des témoignages de Craig Thiel, Toby Thiel et Paul Housen concernant le degré d'ébriété de M. Nikolaisen constituent la seule autre preuve testimoniale sur le lien de causalité. Bien que leurs témoignages aient fourni quelques éléments de preuve touchant cette question, il ne s'agit pas, pour des raisons que j'examinerai plus loin, d'éléments sur lesquels la juge de première instance pouvait raisonnablement s'appuyer. Je n'estime pas non plus qu'elle pouvait se fonder sur la preuve que M. Nikolaisen avait réussi à prendre le virage permettant d'accéder au chemin Snake Hill depuis l'entrée des Thiel. L'inférence que la juge de première instance a tirée de ce fait était déraisonnable et faisait abstraction de la preuve selon laquelle

road three times in the 18 to 20 hours preceding the accident.

I cannot agree with the trial judge that the testimony of Mr. Laughlin, a forensic alcohol specialist employed by the RCMP supports the finding that Mr. Nikolaisen would have reacted to a sign forewarning of the impending right-turning curve on which the accident occurred. The preponderance of Mr. Laughlin's testimony establishes that persons at the level of impairment which Mr. Nikolaisen was found to be at when the accident occurred would be unlikely to react to a warning sign. In addition, Mr. Laughlin's testimony points overwhelmingly to the conclusion that alcohol was the causal factor which led to this accident. The trial judge erred by misapprehending one comment in Mr. Laughlin's testimony and ignoring the significance of his testimony when taken as a whole.

Based on blood samples obtained by Constable Forbes approximately three hours after the accident occurred, Mr. Laughlin predicted that Mr. Nikolaisen's blood alcohol level at the time of the accident ranged from 180 to 210 milligrams percent. Mr. Laughlin commented at length on the effect that this level of blood alcohol could be expected to have on a person's ability to drive, testifying:

> Well, My Lady, this alcohol level that I've calculated here is a very high alcohol level. The critical mental faculties [that] are important in operating a motor vehicle will be impaired by the alcohol. And any skill that depends on these mental faculties will be affected. These include anticipation, judgment, attention, concentration, the ability to divide attention among two or more areas of interest. Because these are affected to such a degree, it would be unsafe for anybody to operate a motor vehicle with this level of alcohol in their body.

le véhicule de M. Nikolaisen avait fait une embardée même dans cette courbe. En outre, la juge de première instance a clairement commis une erreur en ne prenant pas en considération d'autres éléments de preuve pertinents concernant le lien de causalité, en particulier le fait que M. Nikolaisen avait roulé à trois reprises sur le chemin en question au cours des 18 à 20 heures ayant précédé l'accident.

161 Je ne partage pas l'avis de la juge de première instance voulant que le témoignage de M. Laughlin, spécialiste judiciaire en matière d'alcool au service de la GRC, étaye la conclusion que M. Nikolaisen aurait réagi à un panneau lui signalant l'imminence du virage droite où s'est produit l'accident. Le témoignage de M. Laughlin établit de façon prépondérante que des personnes dans un état d'ébriété aussi avancé que celui de M. Nikolaisen au moment de l'accident ne réagiraient vraisemblablement pas à un panneau d'avertissement. De plus, le témoignage de M. Laughlin mène irrésistiblement à la conclusion que l'alcool a été le facteur causal de l'accident. La juge de première instance a commis une erreur à cet égard, car elle a mal interprété un élément de la déposition de M. Laughlin et elle a omis de tenir compte de l'importance de son témoignage, considéré globalement.

162 À la lumière des échantillons de sang prélevés par la gendarme Forbes environ trois heures après l'accident, M. Laughlin a estimé que, au moment de l'accident, l'alcoolémie de M. Nikolaisen se situait entre 180 et 210 mg par 100 ml de sang. Dans son témoignage, M. Laughlin a commenté en détail l'incidence d'une telle alcoolémie sur la capacité d'une personne de conduire :

> [TRADUCTION] Bien, Madame, l'alcoolémie que j'ai calculée en l'espèce est très élevée. Les facultés mentales essentielles qui jouent un rôle important dans la conduite d'un véhicule automobile sont affaiblies par l'alcool. Et toute habileté tributaire de ces facultés mentales est affectée, notamment l'anticipation, le jugement, l'attention, la concentration, la capacité de partager son attention entre deux choses ou plus. Et parce qu'elles sont affectées à ce point, il serait risqué pour quiconque possède un tel taux d'alcool dans son sang de conduire un véhicule automobile.

When asked about his knowledge of research pertaining to the effects of alcohol on the risk of being involved in an automobile accident, Mr. Laughlin had this to say:

> At this level the moderate user of alcohol risk of causing crash is tremendously high, probably 100 times that of a sober driver, or even higher. And in some cases at this level, I've seen scientific literature indicating that the risk of causing a fatal crash is 2 to 300 times that of a sober driver. . . . if an impaired person is an experienced drinker there — it won't be that high. However, there will be an increased risk compared to a sober state. . . . But above 100 milligrams percent, regardless of tolerance, a person will be impaired with respect to driving ability.

Interrogé sur l'état des recherches touchant l'incidence de l'alcool sur le risque d'accident automobile, voici ce qu'a dit M. Laughlin :

> [TRADUCTION] À ce taux-là, le risque qu'une personne qui consomme modérément de l'alcool provoque un accident est extrêmement élevé, probablement 100 fois plus élevé que le conducteur à jeun, ou plus encore. Et dans certains cas, à ce taux-là, j'ai lu des textes scientifiques dans lesquels on indiquait que le risque de provoquer un accident mortel est de 200 à 300 fois plus élevé que celui d'un conducteur à jeun. [. . .] [S]i la personne en état d'ébriété est quelqu'un qui a l'habitude de boire, le risque n'est pas aussi élevé. Cependant, il est plus grand que si la personne avait été à jeun. [. . .] Mais au dessus de 100 mg par 100 ml de sang, peu importe le degré de tolérance à l'alcool, une personne a les facultés affaiblies pour ce qui concerne sa capacité de conduire.

Following these comments, Mr. Laughlin discussed the ability of a severely impaired person to react to the presence of a hazard when driving:

> My Lady, I would like to add that the driving task is a demanding one and involves many multi-various tasks occurring at the same time. The hazard for a person under the influence of alcohol is it takes longer to notice a hazard or danger if one should occur; it takes longer to decide what corrective action is appropriate, and it takes longer to execute that decision and the person may tend to make incorrect decisions. So there is increased risk in that process. As well, if the impairment has progressed to the point where the motor skills are affected, the execution of that decision is impaired. So it's not a very graceful attempt at a corrective action. As well, some people tend to make more risks under the influence of alcohol. They do not apply sound reasoning and judgment. They are not able to properly assess the impairment of their driving skills, they are not able to properly assess the risk, not able to properly assess the changing road and weather conditions and adjust for that. But even if they do recognize those as hazards, they may tend to take more risks than a sober driver would.

Après avoir fait ces remarques, M. Laughlin a décrit la capacité d'une personne en état d'ébriété avancé de réagir à la présence d'un danger lorsqu'elle conduit.

> [TRADUCTION] Madame, j'aimerais ajouter que conduire un véhicule est une activité exigeante, qui demande d'accomplir une multiplicité de tâches simultanément. Le danger pour la personne qui conduit en état d'ébriété réside dans le fait qu'il lui faut plus de temps pour déceler la présence d'un risque ou d'un danger; il lui faut plus de temps pour décider quelle mesure corrective est requise, et elle prend plus de temps à mettre cette décision à exécution; de plus, une telle personne peut avoir tendance à prendre de mauvaises décisions. Ce processus accroît donc le risque. Aussi, si l'ébriété est avancée au point où les habiletés motrices sont affaiblies, l'exécution de la décision s'en trouve compromise. Il s'ensuit donc une tentative plutôt malhabile de corriger la situation. De plus, certaines personnes tendent à prendre davantage de risques lorsqu'elles sont en état d'ébriété. Elles ne font pas preuve de discernement et de jugement. Elles sont incapables d'évaluer correctement les changements dans l'état de la route et les conditions météorologiques et d'adapter leur conduite en conséquence. Mais même si elles reconnaissent qu'il s'agit effectivement de dangers, elles peuvent avoir tendance à prendre davantage de risques que le conducteur à jeun.

163 The above comments support the conclusion that the accident occurred as a result of Mr. Nikolaisen's impairment and not as a result of any failure on the part of the respondent. Indeed, when the portions of Mr. Laughlin's testimony that the trial judge relied

Les remarques qui précèdent étayent la conclusion que l'accident s'est produit en raison de l'état d'ébriété de M. Nikolaisen et non de quelque manquement de la part de l'intimée. De fait, lorsque les extraits du témoignage de M. Laughlin sur lesquels

on are considered in their context, they do not support her conclusion that Mr. Nikolaisen would have been able to react to a sign had one been posted. When asked by counsel whether it was possible for an individual with Mr. Nikolaisen's blood alcohol level to perceive and react to a road sign, Mr. Laughlin responded:

> Yes, it's possible that a person will see and react to it and maybe react properly. It's possible that they will react improperly or may miss it altogether. I think what's key here is that at this level of alcohol, it's more likely that the person under this level of alcohol will either miss the sign or not react properly compared to the sober driver. That the driver with this level of alcohol will make more mistakes than will the sober driver. [Emphasis added.]

In the passage above, it is clear that Mr. Laughlin is merely admitting that anything is possible, while solidly expressing the view that drivers at this level of intoxication are more likely to not react to a sign or other warning. This view is also apparent in the following passage, in which Mr. Laughlin expands on the ability of an intoxicated driver to react to signs and other road conditions:

> What happens with respect to perception under the influence of alcohol is a driver tends to concentrate on the central field of vision, and miss certain indicators on the periphery, that's called tunnel vision. As well, drivers tend to concentrate on the lower part of that central field of view and therefore they don't have a very long preview distance in the course of operating a motor vehicle and looking down the road. And so studies indicate that under the influence of alcohol drivers tend to miss more signs, warnings, indicators, especially those in the peripheral field of view or farther down the road. [Emphasis added.]

In argument before this Court, the appellant emphasized that although Mr. Laughlin was the only expert to testify with respect to causation, lay witnesses testified that Mr. Nikolaisen was not visibly impaired prior to leaving the Thiel residence.

s'est fondée la juge de première instance sont examinés dans leur contexte, ils n'appuient pas la conclusion de cette dernière que M. Nikolaisen aurait été capable de réagir à un panneau de signalisation s'il y en avait eu un. Répondant à la question d'un avocat lui demandant s'il était possible qu'une personne ayant l'alcoolémie de M. Nikolaisen voit un panneau de signalisation et y réagisse, M. Laughlin a dit ceci :

> [TRADUCTION] Oui, il est possible qu'une personne le voit et y réagisse et peut-être qu'elle réagisse adéquatement. Il est possible qu'elle ne réagisse pas adéquatement ou qu'elle ne le voit même pas. J'estime que l'élément fondamental à retenir ici est qu'il est probable que la personne ayant atteint cette alcoolémie ne voit pas le panneau, ou ne réagisse pas adéquatement, comparativement au conducteur à jeun. Que le conducteur avec cette alcoolémie commette plus d'erreurs que le conducteur à jeun. [Je souligne.]

Il est clair, dans le passage qui précède, que M. Laughlin reconnaît simplement que tout est possible, tout en avançant avec conviction qu'il y a une plus forte probabilité que les conducteurs ayant atteint ce degré d'ébriété ne réagissent pas à un panneau de signalisation ou à une autre mesure d'avertissement. Cette opinion ressort également clairement de l'extrait suivant, où il donne des précisions supplémentaires sur la capacité d'une personne en état d'ébriété de réagir aux panneaux de signalisation et à d'autres éléments sur les routes :

> [TRADUCTION] Sur le plan de la perception, le conducteur en état d'ébriété a tendance à se concentrer sur son champ visuel central et à manquer certains indices en périphérie, c'est ce qu'on appelle la vision tubulaire. En outre, les conducteurs ont tendance à se concentrer sur la partie inférieure de ce champ visuel central et, en conséquence, ils ne voient pas très loin devant eux sur la route lorsqu'il sont au volant. Et, par conséquent, les recherches indiquent que les conducteurs en état d'ébriété ont tendance à manquer davantage de panneaux de signalisation, d'avertissements, d'indices, particulièrement ceux situés dans leur champ visuel périphérique ou plus loin sur la route. [Je souligne.]

Au cours des plaidoiries devant notre Cour, l'appelant a souligné que, bien que M. Laughlin ait été le seul expert entendu au sujet du lien de causalité, les témoins ordinaires ont attesté que M. Nikolaisen n'avait pas les facultés visiblement

It is not clear from the trial judge's reasons that she relied on testimony to this effect given by Craig Thiel, Toby Thiel and Paul Housen. To the extent that she did rely on such evidence to establish that the accident was caused in part by the respondent's negligence, I find this reliance to be unreasonable. Whereas the lay witnesses in this case were qualified to give their opinion on whether they, as ordinary drivers, could safely negotiate the segment of Snake Hill Road on which the accident occurred, they were not qualified to assess the degree of Mr. Nikolaisen's impairment. The reason for their lack of qualification in this regard was explained by Mr. Laughlin in the following response to counsel's question on whether it is possible to draw a conclusion from the fact that an individual does not exhibit any impairment of their motor skills and speech:

> No, Your Honour, because, My Lady, when you're looking at motor skill impairment or for signs of motor skill impairment, you're looking for signs of intoxication, not impairment. Remember I mentioned that the first components affected by alcohol are cognitive and mental faculties. These are all important in driving. However, it is very difficult when you look at an individual who has been consuming alcohol to tell that they have impaired in attention or divided attention, or concentration, or judgment. So as an indicator of impairment, motor skills are not reliable. And if you think about the *Criminal Code* process, they've been abandoned 30 years ago as a useful indicator of impairment. No longer do we rely on police officers subjective assessment of person's motor skills to determine impairment. [Emphasis added.]

165 It is also clear from the trial judge's reasons that she relied to some extent on evidence that Mr. Nikolaisen successfully negotiated the curve at the point where the driveway to the Thiel residence intersected the road. I agree with the respondent that this fact is simply not relevant. The ability of Mr. Nikolaisen to negotiate this curve does not establish that his driving ability was not impaired. As noted by the respondent, at para. 101 of its factum, he may

affaiblies avant de quitter la résidence des Thiel. Les motifs de la juge de première instance n'indiquent pas clairement si elle s'est appuyée sur les témoignages de Craig Thiel, Toby Thiel et Paul Housen à cet égard. Dans la mesure où elle se serait fondée sur cette preuve pour conclure que l'accident avait été causé en partie par la négligence de l'intimée, j'estime qu'il était déraisonnable de le faire. En l'espèce, bien que compétents pour exprimer leur opinion sur la question de savoir s'ils pourraient, en tant que conducteurs moyens, manœuvrer en toute sécurité sur le tronçon du chemin Snake Hill où l'accident s'est produit, les témoins ordinaires n'étaient pas compétents pour évaluer le degré d'ébriété de M. Nikolaisen. La raison de leur absence de compétence à cet égard a été expliquée en ces termes par M. Laughlin, dans la réponse suivante qu'il a donnée à l'un des avocats qui lui demandait s'il était possible de tirer des conclusions du fait qu'une personne ne démontre ni signe d'affaiblissement de ses habiletés motrices ni problème d'élocution :

> [TRADUCTION] Non, votre Honneur, puisque, Madame, lorsqu'on vérifie s'il y a affaiblissement des habiletés motrices ou des signes de cet affaiblissement, on cherche des indices d'ébriété, et non d'affaiblissement des facultés. Rappelez-vous que j'ai dit que les premières facultés affectées par l'alcool sont les facultés cognitives et mentales. Elles sont toutes importantes lorsqu'il s'agit de conduire un véhicule. Cependant, lorsqu'on examine une personne qui a consommé de l'alcool, il est très difficile de dire si son attention ou sa capacité de diviser son attention, ou si sa concentration ou son jugement sont réduits. En conséquence les habiletés motrices ne sont pas des indices fiables d'affaiblissement des facultés. Et si on pense au processus prévu par le *Code criminel*, on a cessé d'y recourir depuis 30 ans en tant qu'indices utiles de l'affaiblissement des facultés. On ne se fie plus à l'appréciation subjective policier quant aux habiletés motrices d'une personne pour déterminer si les facultés de celle-ci sont affaiblies. [Je souligne.]

Il appert également des motifs de la juge de première instance qu'elle s'est dans une certaine mesure fondée sur la preuve indiquant que M. Nikolaisen avait réussi à prendre le virage à l'intersection de l'entrée de la résidence des Thiel et du chemin Snake Hill. Je partage l'avis de l'intimée selon lequel ce fait n'est tout simplement pas pertinent. La capacité de M. Nikolaisen de prendre ce virage n'établit pas que sa capacité de conduire

have been driving more slowly at this point, or he may simply have been lucky. More importantly, this evidence contributes nothing to the issue of whether or not Mr. Nikolaisen would have reacted to a sign on the curve where the accident occurred, had one been present. There was no sign on the curve one faces upon leaving the driveway, just as there was no sign on the curve where the accident took place.

n'était pas affaiblie. Comme l'a souligné l'intimée, au par. 101 de son mémoire, il a pu réduire sa vitesse à cet endroit, ou simplement avoir eu de la chance. Facteur plus important encore cette preuve n'aide d'aucune façon à déterminer si M. Nikolaisen aurait réagi à un panneau placé à l'approche de la courbe où s'est produit l'accident, si un tel panneau avait existé. Il n'y avait aucun panneau aux abords de la courbe située à la sortie de l'entrée, tout comme il n'y en avait pas aux abords de celle où s'est produit l'accident.

At any rate, the trial judge's reliance on Mr. Nikolaisen's successful negotiation of the curve at the location of the Thiel driveway ignores relevant evidence that he had swerved or "fish-tailed" when leaving the Thiel residence. A reasonable inference to be drawn from this evidence is that while Mr. Nikolaisen was able to negotiate this curve, he did not do so free from difficulty. While this evidence may not be significant in and of itself, it should have been enough to alert the trial judge to the problems inherent in the inference she drew from his ability to navigate this earlier curve.

166 Quoi qu'il en soit, en se fondant sur le fait que M. Nikolaisen avait pris avec succès le virage devant l'entrée des Thiel, la juge de première instance a fait abstraction de l'élément de preuve pertinent indiquant que l'arrière de son véhicule avait zigzagué à son départ de la résidence des Thiel. On peut raisonnablement inférer de cette preuve que, quoique M. Nikolaisen ait été en mesure de prendre ce virage, il n'y est pas parvenu sans difficulté. Bien que cette preuve ne soit pas nécessairement importante en soi, elle aurait dû néanmoins alerter la juge de première instance quant aux problèmes intrinsèques de l'inférence qu'elle tirait de la capacité de M. Nikolaisen de prendre ce premier virage.

In addition to ignoring the relevant evidence of the fish-tail marks, the trial judge failed to consider the relevance of the fact that Mr. Nikolaisen had travelled Snake Hill Road three times in the 18 to 20 hours preceding the accident. In her review of the evidence, she noted at para. 8 of her reasons that: "Mr. Nikolaisen was unfamiliar with Snake Hill Road. While he had in the preceding 24 hours travelled the road three times, only once was in the same direction that he was travelling upon leaving the Thiel residence."

167 En plus de ne pas avoir tenu compte de la preuve pertinente que constituaient les traces des zigzags, la juge de première instance n'a pas considéré pertinent le fait que M. Nikolaisen avait circulé sur le chemin Snake Hill à trois reprises au cours des 18 à 20 heures ayant précédé l'accident. Dans son examen de la preuve, elle a souligné, au par. 8 de ses motifs, que [TRADUCTION] « M. Nikolaisen ne connaissait pas bien le chemin Snake Hill. Bien qu'il ait emprunté ce chemin à trois reprises au cours des 24 heures précédentes, il ne l'a fait qu'une seule fois dans la même direction que celle qu'il a prise en quittant la résidence des Thiel. »

I simply cannot see how the trial judge found accidents which occurred when motorists were travelling in the opposite direction relevant to the issue of the respondent's knowledge of a risk to motorists while at the same time suggesting that the fact that Mr. Nikolaisen had driven the road in the opposite direction twice was irrelevant to the issue of whether

168 Je ne vois tout simplement pas comment la juge de première instance a pu conclure que les accidents qu'ont eu des automobilistes circulant en sens inverse étaient pertinents pour statuer sur la connaissance par l'intimée de l'existence d'un risque d'accident, tout en suggérant du même souffle que le fait que M. Nikolaisen ait roulé à deux reprises

or not he would have recognized that the curve posed a risk or that he would have reacted to a warning sign. This discrepancy aside, I find the fact that Mr. Nikolaisen had travelled Snake Hill Road in the same direction when he left the Thiel residence to go to the Jamboree the evening before the accident highly relevant to the causation issue. The finding that the outcome would have been different had Mr. Nikolaisen been forewarned of the curve ignores the fact that he already knew that the curve was there. I agree with the respondent that the obvious reason Mr. Nikolaisen was unable to safely negotiate the curve on the afternoon of the 18th, despite having negotiated this curve and others without difficulty in the preceding 18 to 20 hours was the combined effect of his drinking, lack of sleep and lack of food.

169 In conclusion on the issue of causation, I wish to clarify that the fact that the trial judge referred to some evidence to support her findings on this issue does not insulate those findings from review by this Court. The standard of review for findings of fact is reasonableness, not absolute deference. Such a standard entitles the appellate court to assess whether or not it was clearly wrong for the trial judge to rely on some evidence when other evidence points overwhelmingly to the opposite conclusion. The logic of this approach was aptly explained by Kerans, *supra*, in the following passage at p. 44:

> The key to the problem is whether the reviewer is to look merely for "evidence to support" the finding. Some evidence might indeed support the finding, but other evidence may point overwhelmingly the other way. A court might be able to say that reliance on the "some" in the face of the "other" was not what the reasonable trier of fact would do; indeed, it might say that, in all the circumstances it was convinced that to rely on the one in the face of the other was quite unreasonable. To say that "some evidence" is enough, then, without regard to that "other

en sens inverse sur le chemin en question n'était pas pertinent pour déterminer s'il aurait reconnu que la courbe présentait un risque ou s'il aurait réagi à un panneau d'avertissement. Indépendamment de cette contradiction, j'estime que le fait que M. Nikolaisen ait roulé dans la même direction sur le chemin Snake Hill après avoir quitté la résidence des Thiel pour se rendre au jamboree, la veille de l'accident, est fort pertinent en ce qui concerne le lien de causalité. La conclusion que le résultat aurait été différent si une signalisation avait prévenu M. Nikolaisen de l'existence de la courbe ne tient pas compte du fait qu'il savait déjà qu'elle existait. Je souscris à l'opinion de l'intimée que la raison évidente pour laquelle M. Nikolaisen n'a pas réussi à prendre le virage en toute sécurité dans l'après-midi du 18, alors qu'il avait déjà pris ce virage et d'autres sans difficulté au cours des 18 à 20 heures précédentes, était l'effet combiné de sa consommation d'alcool, de son manque de sommeil et du fait qu'il n'avait pas mangé.

Pour conclure sur la question du lien de causalité, j'aimerais préciser que le fait que la juge de première instance ait mentionné certains éléments de preuve au soutien de ses conclusions sur ce point n'a pas pour effet de soustraire ces conclusions au pouvoir de contrôle de notre Cour. La norme de contrôle applicable aux conclusions de fait est celle de la décision raisonnable et non celle de la retenue absolue. Cette norme permet au tribunal d'appel de se demander si le juge de première instance a clairement fait erreur en décidant comme il l'a fait sur le fondement de certains éléments de preuve alors que d'autres éléments mènent irrésistiblement à la conclusion inverse. Kerans, *op. cit.*, p. 44, a habilement exposé la logique de cette démarche dans le passage suivant :

> [TRADUCTION] La solution au problème réside dans la réponse à la question de savoir si le tribunal de révision doit simplement se demander s'il existe « des éléments de preuve étayant » la conclusion. Il est possible que certains éléments de preuve étayent effectivement la conclusion alors que d'autres éléments conduisent irrésistiblement à la conclusion inverse. Un tribunal pourrait être en mesure de dire qu'un juge des faits raisonnable ne s'appuierait pas sur « certains » éléments vu l'existence des « autres »; de fait, il pourrait dire que, eu égard à

evidence" is to turn one's back on review for reasonableness.

D. *Did the Courts Below Err in Finding that no Common Law Duty of Care Exists Alongside the Statutory Duty Imposed Under Section 192 of The Rural Municipality Act, 1989?*

The appellant urges this Court to find that a common law duty of care exists alongside the statutory duty of care imposed on the respondent by s. 192 of *The Rural Municipality Act, 1989*. According to the appellant, the application of the common law duty of care would free the Court from the need to focus on how a reasonable driver exercising ordinary care would have navigated the road in question. The appellant submits that the Court would instead apply the "classic reasonableness formulation" which, in its view, would require the Court to take into account the likelihood of a known or foreseeable harm, the gravity of that harm, and the burden or cost of preventing that harm. The appellant argues that the respondent would be held liable under this test.

The courts below rejected the above argument when it was put to them by the appellant. I would not interfere with their ruling on this issue for the reason that it is unnecessary for this Court to impose a common law duty of care where a statutory one clearly exists. In any event, the application of the common law test would not affect the outcome in these proceedings.

I agree with the respondent's submissions that in this case, where the legislature has clearly imposed a statutory duty of care on the respondents, it would be redundant and unnecessary to find that a common law duty of care exists. The two-part test to establish a common law duty of care set out in *Kamloops (City of) v. Nielsen*, [1984] 2 S.C.R. 2, simply has no application where the legislature has defined a statutory duty. As was stated by this Court in *Brown*

l'ensemble des circonstances, il est convaincu qu'il était tout à fait déraisonnable de se fonder sur certains éléments compte tenu des autres. En conséquence, affirmer que « certains éléments de preuve » suffisent, sans égard aux « autres éléments », revient à abandonner l'examen du caractère raisonnable.

D. *Les juridictions inférieures ont-elles commis une erreur en concluant qu'aucune obligation de diligence de common law ne coexiste avec l'obligation légale imposée par l'art. 192 de la Rural Municipality Act, 1989?*

170 L'appelant invite notre Cour à conclure qu'une obligation de diligence de common law coexiste avec l'obligation légale de diligence imposée à l'intimée par l'art. 192 de la *Rural Municipality Act, 1989*. Selon l'appelant, l'application de l'obligation de diligence de common law dispenserait la Cour de la nécessité de se demander comment un conducteur raisonnable prenant des précautions normales aurait roulé sur le chemin en cause. L'appelant soutient que la Cour pourrait plutôt appliquer le [TRADUCTION] « critère classique de la conduite raisonnable », lequel, à son avis, l'obligerait à tenir compte des éléments suivants : la probabilité qu'un préjudice connu ou prévisible survienne, la gravité de ce préjudice et le fardeau ou le coût qu'il faudrait assumer pour le prévenir. L'appelant prétend que, suivant ce critère, l'intimée serait tenue responsable.

171 Les juridictions inférieures ont rejeté l'argument susmentionné de l'appelant. Je ne modifierais pas leur décision sur cette question, car il est inutile que notre Cour impose une obligation de diligence de common law lorsqu'il existe clairement une obligation d'origine législative. Quoi qu'il en soit, l'application du critère prévu par la common law ne modifierait pas l'issue de la présente instance.

172 Je souscris à l'argument de l'intimée selon lequel, en l'espèce, il serait redondant et inutile de conclure qu'elle est assujettie à une obligation de diligence de common law alors que le législateur lui a clairement imposé une obligation légale de diligence. Le critère à deux volets énoncé dans l'arrêt *Kamloops (Ville de) c. Nielsen*, [1984] 2 R.C.S. 2, pour statuer sur l'existence d'une obligation de diligence de common law, ne s'applique tout

v. British Columbia (Minister of Transportation and Highways), [1994] 1 S.C.R. 420, at p. 424:

> . . . if a statutory duty to maintain existed as it does in some provinces, it would be unnecessary to find a private law duty on the basis of the neighbourhood principle in *Anns v. Merton London Borough Council*, [1978] A.C. 728. Moreover, it is only necessary to consider the policy/operational dichotomy in connection with the search for a private law duty of care.

All of the authorities cited by the appellant as support for the imposition of an independent common law duty of care can be distinguished from the case at hand on the basis that no statutory duty of care existed (*Just*, *supra*; *Brown*, *supra*; *Swinamer v. Nova Scotia (Attorney General)*, [1994] 1 S.C.R. 445; *Ryan*, *supra*).

173 In addition, I find that the outcome in this case would not be different if the case were determined according to ordinary negligence principles. First, were the Court to engage in a common law analysis, it would still look to the statutory standard of care as laid out in *The Rural Municipality Act, 1989*, as interpreted by the case law in order to assess the scope of liability owed by the respondent to the appellant. As this Court stated in *Ryan*, *supra*, at para. 29:

> Statutory standards can, however, be highly relevant to the assessment of reasonable conduct in a particular case, and in fact may render reasonable an act or omission which would otherwise appear to be negligent. This allows courts to consider the legislative framework in which people and companies must operate, while at the same time recognizing that one cannot avoid the underlying obligation of reasonable care simply by discharging statutory duties.

174 Moreover, even under the common law analysis, this Court would be called upon to question the type of hazards that the respondent, in this case, ought to have foreseen. Whatever the approach, it is only reasonable

simplement pas lorsque le législateur a prescrit l'obligation dans la loi. Comme l'a indiqué notre Cour dans l'arrêt *Brown c. Colombie-Britannique (Ministre des Transports et de la Voirie)*, [1994] 1 R.C.S. 420, p. 424 :

> . . . s'il existait une obligation d'entretien imposée par la loi comme c'est le cas dans certaines provinces, il serait inutile de rechercher une obligation en droit privé en se fondant sur le principe du prochain établi dans l'arrêt *Anns c. Merton London Borough Council*, [1978] A.C. 728. En outre, il est nécessaire d'examiner la dichotomie politique générale-opérations seulement en ce qui concerne la recherche d'une obligation de diligence en droit privé.

Tous les arrêts invoqués par l'appelant pour justifier sa prétention que la municipalité devrait être assujettie à une obligation indépendante de diligence de common law peuvent être distingués de la présente affaire, étant donné qu'il n'existait aucune obligation légale de diligence dans ces affaires (*Just*, précitée; *Brown*, précitée; *Swinamer c. Nouvelle-Écosse (Procureur général)*, [1994] 1 R.C.S. 445; *Ryan*, précitée).

En outre, j'estime que le résultat serait le même en l'espèce si l'affaire était tranchée d'après les principes ordinaires de la négligence. Tout d'abord, si la Cour faisait l'analyse prévue par la common law, elle appliquerait quand même la norme légale de diligence établie dans la *Rural Municipality Act, 1989*, telle qu'elle a été interprétée par la jurisprudence, pour déterminer l'étendue de la responsabilité de l'intimée envers l'appelant. Comme l'a dit notre Cour dans l'arrêt *Ryan*, précité, par. 29 :

> Cependant, les normes législatives peuvent être hautement pertinentes pour déterminer ce qui constitue une conduite raisonnable dans un cas particulier, et elles peuvent, en fait, rendre raisonnable un acte ou une omission qui, autrement, paraîtrait négligent. En conséquence, les tribunaux peuvent examiner le cadre législatif dans lequel les personnes et les sociétés doivent agir, tout en reconnaissant qu'il est impossible de se soustraire à l'obligation sous-jacente de diligence raisonnable simplement en s'acquittant de ses obligations légales.

De plus, même dans le cadre de l'analyse requise par la common law, notre Cour devrait s'interroger sur le type de dangers que l'intimée aurait dû prévoir en l'espèce. Indépendamment de l'approche choisie,

sonable to expect a municipality to foresee accidents which occur as a result of the conditions of the road, and not, as in this case, as a result of the condition of the driver.

The courts have long restricted the standard of care under the statutory duty to require municipalities to repair only those hazards which would pose a risk to the reasonable driver exercising ordinary care. Compelling reasons exist to maintain this interpretation. The municipalities within the province of Saskatchewan have some 175,000 kilometres of roads under their care and control, 45,000 kilometres of which fall within the "bladed trail" category. These municipalities, for the most part, do not boast large, permanent staffs with extensive time and budgetary resources. To expand the repair obligation of municipalities to require them to take into account the actions of unreasonable or careless drivers when discharging this duty would signify a drastic and unworkable change to the current standard. Accordingly, it is a change that I would not be prepared to make.

VII. Disposition

In the result, the judgment of the Saskatchewan Court of Appeal is affirmed and the appeal is dismissed with costs.

Appeal allowed with costs, GONTHIER, BASTARACHE, BINNIE *and* LEBEL JJ. *dissenting.*

Solicitors for the appellant: Robertson Stromberg, Saskatoon; Quon Ferguson MacKinnon, Saskatoon.

Solicitors for the respondent: Gerrand Rath Johnson, Regina.

il n'est que raisonnable d'attendre d'une municipalité qu'elle prévoit les accidents qui surviennent en raison de l'état du chemin, et non, comme en l'espèce, ceux qui résultent de l'état du conducteur.

175 Depuis longtemps, les tribunaux limitent l'étendue de la norme de diligence découlant de l'existence d'un devoir légal de diligence à l'obligation pour les municipalités d'éliminer seulement les dangers qui présenteraient un risque pour le conducteur raisonnable prenant des précautions normales. Des raisons impérieuses militent en faveur du maintien de cette interprétation. Les municipalités de la province de la Saskatchewan assument l'entretien et la surveillance de quelque 175 000 kilomètres de route, dont 45 000 kilomètres font partie de la catégorie des « chemins nivelés ». La plupart de ces municipalités ne disposent ni d'effectifs permanents considérables ni de ressources importantes en temps et en argent. Élargir l'obligation d'entretien des municipalités en exigeant qu'elles tiennent compte, dans l'exécution de cette obligation, des actes des conducteurs déraisonnables ou imprudents, entraînerait une modification radicale et irréalisable de la norme actuelle. Il s'agit en conséquent d'un changement que je ne serais pas disposé à apporter.

VII. Dispositif

176 En définitive, le jugement de la Cour de l'appel de la Saskatchewan est confirmé et le pourvoi est rejeté avec dépens.

Pourvoi accueilli avec dépens, les juges GONTHIER, BASTARACHE, BINNIE *et* LEBEL *sont dissidents.*

Procureurs de l'appelant : Robertson Stromberg, Saskatoon; Quon Ferguson MacKinnon, Saskatoon.

Procureurs de l'intimée : Gerrand Rath Johnson, Regina.

TAB 6

COURT OF APPEAL FOR ONTARIO

CITATION: Manastersky v. Royal Bank of Canada, 2021 ONCA 458
DATE: 20210624
DOCKET: C65121

Feldman, Brown and Miller JJ.A.

BETWEEN

James Anthony Manastersky

Plaintiff (Respondent)

and

Royal Bank of Canada and RBC Dominion Securities Inc.

Defendant (Appellant)

Jeremy Devereux and Geoff Mens, for the appellant

Nancy Shapiro, for the respondent

Heard: January 19, 2021 by video conference

On remand from the Judgment of the Supreme Court of Canada dated November 12, 2020.

Brown J.A.:

I. OVERVIEW

[1] This remand from the Supreme Court of Canada involves the award of certain incentive plan-related damages to the respondent, Mr. James Anthony Manastersky, in his wrongful dismissal action against his employer, the appellant RBC Dominion Securities Inc. ("RBCDS"). At trial, RBCDS conceded that it had

terminated Mr. Manastersky's employment without cause. The trial judge found that Mr. Manastersky was entitled to 18 months' reasonable notice upon termination: 2018 ONSC 966, 46 C.C.E.L. (4th) 316.

[2] During his employment, Mr. Manastersky participated in profit-sharing plans called "carried interest plans". From late 2004 until his termination in 2014, Mr. Manastersky participated in the Mezzanine Carried Interest Plan (the "Mezzanine CIP"). The trial judge awarded Mr. Manastersky: (i) the sum of $953,392.50 in respect of "the lost opportunity to earn entitlements under" the Mezzanine CIP during the 18-month reasonable notice period: Judgment, para. 5; and (ii) the amount of $190,789.00 in respect of Mr. Manastersky's share of investment proceeds under the Mezzanine CIP for the period 2005 to 2013, as calculated using Mr. Manastersky's foreign exchange methodology: Judgment, para. 6.

[3] RBCDS appealed both parts of the award.

[4] By reasons dated July 18, 2019, this court (Feldman J.A. dissenting) allowed RBCDS' appeal regarding the award of damages in respect of the incentive plan. The court unanimously dismissed the appeal regarding the foreign exchange methodology: 2019 ONCA 609, 146 O.R. (3d) 647 (the "Original Decision").

[5] Mr. Manastersky sought leave to appeal to the Supreme Court of Canada. By Judgment dated November 12, 2020, the Supreme Court remanded the case to this court pursuant to s. 43(1.1) of the *Supreme Court Act*, R.S.C. 1985, c. S-

26, with the direction that “the case forming the basis of the application for leave to appeal” is remanded to this court “for disposition in accordance with *Matthews v. Ocean Nutrition Canada Ltd.*, 2020 SCC 26” (the “Remand Directions”)

[6] This court sought and received remand submissions from the parties and heard oral submissions on January 19, 2021.

II. THE APPROACH ON A REMAND

[7] On the remand of a case from the Supreme Court with directions to dispose of the case in accordance with an identified decision of that court, this court will reconsider its original decision in light of the authoritative pronouncement of the Supreme Court on issues that may have affected this court’s disposition of the appeal. If the application of the identified Supreme Court decision mandates a different disposition, this court should alter its earlier decision in light of the holdings of that decision; if it does not, this court should affirm its earlier decision: *Deslaurier Custom Cabinets Inc. v. 1728106 Ontario Inc.*, 2017 ONCA 293, 135 O.R. (3d) 241, at para. 14, leave to appeal refused, [2016] S.C.C.A. No. 249; *Sankar v. Bell Mobility Inc.*, 2017 ONCA 295, 410 D.L.R. (4th) 1, at para. 9, leave to appeal refused, [2016] S.C.C.A. No. 251; *Mikelsteins v. Morrison Hershfield Limited*, 2021 ONCA 155, at para. 16.

[8] In performing the exercise required by the Remand Directions, I have considered the following: (i) the *Matthews* decision; (ii) the Original Decision; (iii)

the trial judge's reasons; (iv) the portions of the record relevant to the issue raised by the Remand Directions; and (v) the submissions of the parties on the appeal and in respect of the remand hearing. As these reasons address the parties' submissions made on the remand, they supplement and therefore should be read together with the Original Decision.

III. THE LAW AS AFFIRMED IN THE *MATTHEWS* DECISION

[9] Upon the termination of employment without cause, an employee is entitled to damages equivalent to what the employee would have earned during the notice period, including compensation for bonuses or incentives that would have been earned had the employer not breached the employment contract: *Matthews*, at para. 48. The purpose of damages in lieu of reasonable notice is to put employees in the position they would have been in had they continued to work through to the end of the notice period: *Matthews,* at para. 59. The remedy for a breach of the implied term to provide reasonable notice is an award of damages based on the period of notice which should have been given, with the damages representing what the employee would have earned in this period: *Matthews*, at para. 49.

[10] Noting that how payments under incentive bonuses or plans are to be included in these damages is a recurring issue in the law of wrongful dismissal, the Supreme Court affirmed the two-step approach set out by this court in *Lin v. Ontario Teachers' Pension Plan*, 2016 ONCA 619, 402 D.L.R. (4th) 325, *Paquette*

v. TeraGo Networks Inc., 2016 ONCA 618, 352 O.A.C. 1, and *Taggart v. Canada Life Assurance Co.* (2006), 50 C.C.P.B. 163 (Ont. C.A.): at para. 49. The Supreme Court stated, at paras. 52-54, that the two-step approach rests on two key principles:

(i) When employees sue for damages for wrongful dismissal, they are claiming for damages as compensation for the income, benefits, and bonuses they would have received had the employer not breached the implied term to provide reasonable notice; and

(ii) A contract of employment effectively "remains alive" for the purposes of assessing the employee's damages, in order to determine what compensation the employee would have been entitled to but for the dismissal.

[11] Building on those two principles, the Supreme Court, at para. 55, affirmed a two-step approach to determine whether an employee dismissed without cause is entitled to damages in respect of a bonus or incentive benefit:

> Courts should accordingly ask two questions when determining whether the appropriate quantum of damages for breach of the implied term to provide reasonable notice includes bonus payments and certain other benefits. Would the employee have been entitled to the bonus or benefit as part of their compensation during the reasonable notice period? If so, do the terms of the employment contract or bonus plan unambiguously take away or limit that common law right?

[12] The Supreme Court further clarified that resorting to the so-called “integral” test does not play a role in all cases. Where there is doubt about whether the employee would have received a discretionary bonus during the reasonable period of notice, resorting to the test of whether a benefit or bonus is “integral” to the employee’s compensation can assist in answering the question of what the employee would have been paid during the reasonable notice period: *Matthews,* at para. 58. By contrast, where there is no doubt that the employee would have received a bonus or incentive benefit during the notice period, there is no need to ask whether the bonus was “integral” to the employee’s compensation: *Matthews*, at para. 59. At the remand hearing, counsel for Mr. Manastersky acknowledged that, on the facts of this case, the issue of whether the incentive benefit was “integral” does not arise because the entitlement to payments under the Mezzanine CIP was not discretionary.

[13] The Original Decision identified the legal principles applicable to the appeal as those set out in *Lin*, *Paquette*, and *Taggart*, including the application of the two-step approach: Original Decision, paras. 39-43. Consequently, I do not see the exercise on this remand as applying any new legal principles identified in *Matthews* to the case on appeal; the legal principles affirmed in *Matthews* were those applied in the Original Decision. Instead, I propose to look afresh at the application of the two-step analysis to the case on appeal.

IV. THE APPLICATION OF *MATTHEWS'* TWO-STEP ANALYSIS

A. WHAT RBCDS PAID MR. MANASTERSKY ON TERMINATION IN RESPECT OF HIS MEZZANINE CIP ENTITLEMENT

[14] Before reconsidering the application of the two-step approach to the present case, it is worth recalling what compensation RBCDS paid Mr. Manastersky in respect of his legal rights under the Mezzanine CIP following his termination.

[15] The Original Decision described, at paras. 8 to 12, the various incentive plans that had formed part of Mr. Manastersky's employment contract. The details of the Mezzanine CIPs in place at the date of termination are set out at paras. 13 to 22 of the Original Decision. I see no need to repeat them; I incorporate them in these reasons.

[16] RBCDS terminated Mr. Manastersky's employment on February 14, 2014. As of that date, two funds – Funds 1 and 2 – had been established under the Mezzanine CIP. Each fund contained a portfolio of investments for an Investment Period. Mr. Manastersky had been granted points, or shares, in the profits generated by the portfolios of both funds. No profits from either fund had been distributed by the time of Mr. Manastersky's termination; his interests in both funds had been carried from 2008 until 2014. Significant payouts were made after RBCDS gave notice to Mr. Manastersky and wound-up the funds: $3,624,079 in 2015; and $1,810,230 in 2016.

[17] The trial judge found that Mr. Manastersky was entitled to 18-months' notice, which ran from February 14, 2014 until August 14, 2015.

[18] Several months after Mr. Manastersky's termination, RBCDS began to wind-up Funds 1 and 2. It also approved the termination of the Mezzanine CIP in respect of all future Investment Periods – that is to say, no further investment funds would be created within the Mezzanine CIP: Original Decision, at para. 28.

[19] At trial, Mr. Manastersky filed an Updated Earnings Summary. It showed that during 2015 and 2016 he was fully paid his share of the profits from the winding-up of Funds 1 and 2. Mr. Manastersky acknowledged that RBCDS had paid him all profits from Funds 1 and 2 to which he was entitled under the Mezzanine CIP.

[20] The evidence therefore shows that both during and after Mr. Manastersky's period of reasonable notice RBCDS administered the wind-up of Funds 1 and 2 and paid out Mr. Manastersky's share of Fund profits. Put differently, during and after his period of reasonable notice Mr. Manastersky received all the incentive plan benefits to which he was entitled in respect of the two funds that existed at the time of the termination of his employment.

B. ANALYSIS

[21] Under the *Matthews* framework, the issue of any limitations on an employee's entitlement to bonus/incentive benefit compensation typically (but not invariably) would arise under the second step – namely, do the terms of the

employment contract or bonus plan unambiguously take away or limit a common law right or entitlement upon the termination of employment? The factual twist in the present case is that the issue of any limitation on Mr. Manastersky's entitlement to further incentive benefits during his period of reasonable notice falls more under *Matthews'* first step: would he have been entitled to receive payment of a CIP incentive benefit as part of his compensation during the reasonable notice period? However, as recognized in the Original Decision, at para. 51, incentive-benefit plans vary greatly in their structure and pay-out terms, so the analysis in respect of one type of incentive plan may not be transferable to the analysis of another type of incentive plan.

[22] In *Matthews*, the employee's entitlement to a long-term incentive plan payment – the occurrence of a "Realization Event" such as the sale of the employer – was limited by the incentive plan's requirement that the employee be a "full-time employee" at the date of the Realization Event. The Supreme Court held that the first step was clearly satisfied because the Realization Event fell within the employee's reasonable notice period; but for the employee's dismissal, he would have received the incentive payment: *Matthews,* at para. 59. In considering the second step, the Supreme Court held that the language of "full-time employee" did not limit the employee's entitlement to the incentive payment when the Realization Event occurred during the period of reasonable notice: *Matthews*, at paras. 65-67.

[23] The circumstances of the present case differ from those in *Matthews*. Here, the Mezzanine CIP did not place a limit on Mr. Manastersky's entitlement to his carried interest incentives in the event of the termination of his employment without cause. As stated in the Original Decision, at para. 17:

> There is no dispute that at the time of his termination, Mr. Manastersky's points were fully vested. When the employment of a participant was terminated without cause, the participant continued as a participant, retaining "in all Portfolios with respect to which he or she has Points, all rights represented by his or her Vested Points."

[24] Instead, Mr. Manastersky takes issue with the treatment by the majority in the Original Decision of the scope of his entitlement in respect of the Mezzanine CIP incentive benefits during the period of reasonable notice. He contends that he was entitled to more than merely the payment of his share of the profits from Funds 1 and 2.

[25] In applying *Matthews'* first step, the majority in the Original Decision concluded that Mr. Manastersky was entitled to benefits during the period of reasonable notice in respect of Funds 1 and 2 because the terms of the Mezzanine CIP linked his entitlement to incentive benefits to the existence of discrete Investment Periods, each encompassing a specific portfolio in a specific fund. Those terms of the Mezzanine CIP differed from those considered in *Paquette* and *Lin*. As stated in the Original Decision, at paras. 55-56:

> The entitlement of a participant, such as Mr. Manastersky, to earn payments under the Mezzanine CIP was tied to the existence of the funds created for different Investment Periods. Two funds existed during the last decade of Mr. Manastersky's employment and the period of reasonable notice: Funds 1 and 2. In accordance with the terms of the Mezzanine CIP, Mr. Manastersky was allocated a specific amount of points in respect of each Fund.
>
> As Article 4.4 of the Mezzanine CIP clearly stated, the status of a participant with respect to any Investment Period "shall not give any Participant the express or implied right … to any Points for any future Investment Period." [Emphasis added]

[26] The Original Decision went on to state, in part, at paras. 61-62:

> [T]he terms of the Mezzanine CIP provided that Mr. Manastersky was not entitled to any further earnings under that plan:
>
> i. The Management Committee was entitled to "terminate the Plan effective as of the end of any Investment Period with respect to future Investment Periods": Art. 9.3. The Management Committee did so. No new Fund 3 Investment Period was created;
>
> ii. A participant was granted points in respect "to each Portfolio relating to a given Investment Period" and those points represented the Participant's share of the portion of the aggregate profits and losses of RBCDS with respect to that Portfolio: Art. 6.1.1;
>
> iii. Any allocation of points in connection with an Investment Period after the Funds 1 and 2 Investment Periods would be done by way of a new allocation letter: Art. 6.1.3; and
>
> iv. An employee's status as a participant in respect to any Investment Period did not

> give the participant "the express or implied right … to any Points for any future Investment Period": Art. 4.4.
>
> Those provisions, when combined with the decision of the Management Committee to terminate the Plan, indicate that Mr. Manastersky was not entitled to any common law damages in respect of the Mezzanine CIP profit-sharing plan beyond those relating to his vested points for Funds 1 and 2…

[27] Mr. Manastersky contends that analysis was in error. He points to language used in *Matthews*, in respect of the second step of the analysis, that a plan's limitation on entitlement to an incentive payment will not be effective unless it "unambiguously" limits or removes the employee's common law right, is "absolutely clear and unambiguous" or clearly covers the "exact circumstances which have arisen": *Matthews*, at paras. 55 and 64-66.

[28] Drawing on that language, Mr. Manastersky argues that the terms of the Mezzanine CIP that permitted termination of "the Plan effective as of the end of any Investment Period with respect to future Investment Periods" (Art. 9.3) and stipulating that an employee's status as a participant in respect to any Investment Period did not give the participant "the express or implied right … to any Points for any future Investment Period" (Art. 4.4) could not operate to limit his entitlement to incentive compensation, during the period of reasonable notice, to only the payout of his profit shares in Funds 1 and 2. Mr. Manastersky contends that notwithstanding the language defining the scope of his entitlement in the Mezzanine Plan (i.e., his common law right), he is entitled to more because the

provisions of the Mezzanine CIP – Arts. 4.4, 6.1.1, 6.1.3, and 9.3 – did not clearly and unambiguously cover the exact circumstances that arose in his case, namely the termination and winding-up of Funds 1 and 2 during his period of reasonable notice.

[29] Mr. Manastersky advances two bases upon which to calculate the “more” to which he contends he is entitled as further damages for incentive benefits during the notice period.

[30] First, he submits that since, for all intents and purposes, he was the only remaining employee beneficiary of the two funds, RBCDS was required to give him reasonable notice of the termination of the funds equivalent to the 18-months’ reasonable notice found by the trial judge. That would mean RBCDS would have to continue to operate the Mezzanine Funds and make new investments until the end of his period of reasonable notice (August 2015).

[31] I see two difficulties with that submission.

[32] First, in his evidence Mr. Manastersky acknowledged that the Investment Period for Fund 1 ended on December 15, 2006, following the departure of a senior plan member, and the Fund 2 Investment Period effectively came to an end in 2013, prior to Mr. Manastersky’s termination, when its investments reached $158 million. While that was just shy of the $160 million portfolio cap that would end an

Investment Period, further investments in Fund 2 were not practical as the remaining $2 million was smaller than any deal the Mezzanine Fund had done.

[33] Second, there was no evidence adduced at trial that would enable the court to determine whether deferring the process of winding-up Funds 1 and 2 from the summer of 2014 until the end of the notice period in August 2015 would have resulted in a higher payout to Mr. Manastersky of his share of the profits in the funds. Further, as the CIP was a profit-sharing program, there was no guarantee that making further investments would prove profitable and increase Mr. Manastersky's payout.

[34] The second basis for calculating the "more" is the one Mr. Manastersky primarily relied upon at the appeal. At trial, Mr. Manastersky admitted that he was not taking the position that he was entitled to an allocation of points with respect to some new or notional Fund 3 Investment Period that was never established by RBCDS under the Mezzanine CIP.

[35] By taking that position, Mr. Manastersky seemed to acknowledge that the conclusion of one Investment Period under the Mezzanine CIP did not automatically require RBCDS to start a new one, as reflected in Art. 9.3 of the Mezzanine CIP that entitled the Plan's Management Committee to "terminate the Plan effective as of the end of any Investment Period with respect to future Investment Periods."

[36] Notwithstanding that acknowledgement, Mr. Manastersky submits that he is entitled to more than his actual share of profits from the realization of Funds 1 and 2 that he received both during and after the period of reasonable notice. He contends that RBCDS should pay an additional amount in respect of the notice period calculated by averaging the actual share of the profits in Funds 1 and 2 that he received during and after the notice period over the lifetimes of the funds and then applying the resulting annual average (the "Notional Annualized Historical Profit Share") *pro rata* to the 18-month notice period. Under that approach, Mr. Manastersky contends that during the period of reasonable notice he should have received Mezzanine CIP-related incentive benefits made up of two components: (i) first, the payouts of $5,434,309 that RBCDS made to Mr. Manastersky during and after the period of reasonable notice for his share in the profits of Funds 1 and 2, calculated in accordance with the terms of the Mezzanine CIP; plus (ii) an additional $953,392.50 in damages calculated by applying the Notional Annualized Historical Profit Share for those same funds *pro rata* to the 18-month period of reasonable notice.[1]

[37] I remain unpersuaded by that submission. The first step of *Matthews* requires ascertaining whether an employee would have been entitled to an

[1] The trial judge, at paras. 50-51, averaged Mr. Manastersky's CIP entitlement over the period 2005 to 2013 (9 years), calculated a notional annual entitlement from Funds 1 and 2, and the multiplied it by the 1.5 years reasonable notice period.

incentive or benefit as part of their compensation during the reasonable notice period: at para. 55. Determining the content of that common law right requires examining the characteristics of the incentive or benefit to which the employee would be entitled. In many cases, the character of the incentive or benefit will be an annual payment or bonus. But that is not the character of the common law contractual benefit under the Mezzanine CIP. It was a "carried interest" plan that quite clearly did not entitle its participants to annual payments. By its terms, a participant was only entitled to receive a payment at the conclusion of an Investment Period and the realization of a specific fund's investment portfolio. And, as noted, Mr. Manastersky carried his interest in the two funds from 2008 until 2014 without receiving any annual payment; he was paid his share of the profits from the two funds in 2015 and 2016.

[38] To accede to Mr. Manastersky's submission would, in effect, recast his common law, fund-specific entitlement to incentive compensation under the Mezzanine CIP into a notional "annual or annualized" entitlement. The trial judge and my colleague in dissent in the Original Decision acceded to Mr. Manastersky's submission. With respect, I cannot.

[39] Mr. Manastersky's position seeks to alter, in a fundamental way, the character of the common law right to incentive compensation to which he was entitled under his employment contract. The terms of an incentive plan's eligibility criteria and formula for calculating a bonus remain relevant to the inquiry into what

benefit the employee would have been entitled to as part of his or her compensation during the reasonable period of notice: *Paquette*, at para. 18. I do not read the *Matthews* decision as changing that principle.

[40] *Matthews* provides that damages for dismissal are designed to compensate the employee "for the income, benefits, and bonuses they would have received had the employer not breached the implied term to provide reasonable notice:" at para. 53. The terms of Mr. Manastersky's employment contract did not entitle him to receive an annual incentive payment. The terms entitled him to receive a fund-specific incentive payment upon the end of a fund's investment period. During his period of reasonable notice, Mr. Manastersky was entitled to receive damages calculated on the latter basis, not damages calculated on both bases. In my view, RBCDS paid Mr. Manastersky that to which he was entitled at common law and, with respect, the trial judge erred in concluding otherwise.

V. DISPOSITION

[41] For these reasons, having considered the Original Decision in light of *Matthews*, I would affirm the Original Decision.

[42] I would order Mr. Manastersky to pay RBCDS its costs of the remand fixed in the amount of $5,000.00, inclusive of disbursements and applicable taxes.

"David Brown J.A."
"I agree. B.W. Miller J.A."

Feldman J.A. (dissenting):

A. INTRODUCTION

[43] Mr. Manastersky sought leave to appeal this court's majority decision to the Supreme Court of Canada. The issue to be decided was essentially whether the majority's decision overturning the trial judge, or the dissenting reasons that would have upheld the trial judge, had correctly applied the test for damages for wrongful dismissal, as set out in this court's decisions in *Lin v. Ontario Teachers' Pension Plan*, 2016 ONCA 619, 402 D.L.R. (4th) 325, *Paquette v. TeraGo Networks Inc.*, 2016 ONCA 618, 352 O.A.C. 1, and *Taggart v. Canada Life Assurance Co.* (2006), 50 C.C.P.B. 163 (Ont. C.A.).

[44] Before considering whether to grant the appellant leave to appeal, the Supreme Court heard an appeal from the Nova Scotia Court of Appeal in *Matthews v. Ocean Nutrition Canada Ltd.*, 2020 SCC 26, 449 D.L.R. (4th) 583, and reserved its decision. Ultimately, in *Matthews*, the Supreme Court did not change the law of Ontario and endorsed this court's approach in *Lin*, *Paquette*, and *Taggart*.

[45] Without granting leave to appeal, the Supreme Court remanded the appellant's case to this court pursuant to s. 43(1.1) of the *Supreme Court Act*, R.S.C. 1985, c. S-26, "for disposition in accordance with *Matthews v. Ocean Nutrition Canada Ltd.*, 2020 SCC 26."

[46] Because the Supreme Court in *Matthews* adopted and endorsed this court's jurisprudence that had been applied by the trial judge, and by the majority and the dissent on the appeal, both the parties and this court have had to grapple with the question of what issue was remanded to this court for rehearing. To me, the correct approach is to ask the question: If the trial judge had had the benefit of the *Matthews* decision, would he have approached the case differently? Similarly, on appeal, the question for this court would be: Did the trial judge err by failing to apply the principles and the test as now set out by the Supreme Court in *Matthews*?[2]

B. THE *MATTHEWS* DECISION

[47] David Matthews was an experienced chemist who, from 1997, occupied a number of senior management positions with Ocean Nutrition Canada Ltd. ("Ocean"). In 2007, efforts to force Mr. Matthews out of the company started, and he ultimately resigned in 2011, resulting in constructive dismissal.

[48] As a senior executive, Mr. Matthews was part of the long-term incentive plan ("LTIP"), which included as a benefit a significant payment in the event of the sale of the company. About 13 months after Mr. Matthews was forced out, the company

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[2] In *British Columbia (Ministry of Forests) v. Teal Cedar Products Ltd.*, 2015 BCCA 263, 70 B.C.L.R. (5th) 318, at para. 2, the Court of Appeal for British Columbia, considering a remand after the Supreme Court's decision in *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633, stated that the remand hearing was to be treated as a fresh appeal: "Although this Court can inform itself from its earlier reasons, the appeals are to be reconsidered having particular regard for the law as stated in *Sattva*." The remand decision was appealed to the Supreme Court, where the result was overturned: see *Teal Cedar Products Ltd. v. British Columbia*, 2017 SCC 32, [2017] 1 S.C.R. 688. But the Supreme Court stated, at para 78: "However, on remand, the Court of Appeal had the benefit of *Sattva*, and its decision was specifically directed toward reconsidering the majority's decision in light of *Sattva*."

was sold for $540,000,000, but it refused to pay him his entitlement under the LTIP on the basis that he did not comply with a provision that required him to be a "full-time employee" on the date of the sale.

[49] In endorsing this court's decisions in *Lin*, *Paquette*, and *Taggart*, the Supreme Court in *Matthews* made the following important observations, at paras. 47-55, about the purpose of the two-step test for determining a wrongfully dismissed employee's entitlement to damages, and how to apply it:

> [47] In the case at bar, the only disagreement in respect of reasonable notice turns on whether Mr. Matthews' damages include an amount to compensate him for his lost LTIP payment.
>
> [48] In my respectful view, the majority of the Court of Appeal erred by focusing on whether the terms of the LTIP were "plain and unambiguous" instead of asking what damages were appropriately due for Ocean's failure to provide Mr. Matthews with reasonable notice. The issue is not whether Mr. Matthews is entitled to the LTIP in itself, but rather what damages he is entitled to and whether he was entitled to compensation for bonuses he would have earned had Ocean not breached the employment contract. By focusing narrowly on the former question, the Court of Appeal applied an incorrect principle, resulting in what I see as an overriding error.
>
> …
>
> [49] Insofar as Mr. Matthews was constructively dismissed without notice, he was entitled to damages representing the salary, including bonuses, he would have earned during the 15-month period (*Wallace*, at paras. 65-67). This is so because the remedy for a breach of the implied term to provide reasonable notice is an award of damages based on the period of notice

which should have been given, with the damages representing “what the employee would have earned in this period” (para. 115). Whether payments under incentive bonuses, such as the LTIP in this case, are to be included in these damages is a common and recurring issue in the law of wrongful dismissal. To answer this question, the trial judge relied on *Paquette* and *Lin* from the Court of Appeal for Ontario. I believe he took the right approach.

[50] In *Paquette*, the employee participated in his employer’s bonus plan, which stipulated that employees had to be “actively employed” on the date of the bonus payout. That language is broadly comparable to that found in the LTIP which, at clause 2.03, requires the claimant to be a “full-time employee” of the company. In Paquette, but for the employee’s termination, the employee would have received the bonus within the reasonable notice period. The motion judge in that case, however, concluded that the employee was not entitled to the bonus because, while he may have been “notionally” employed during the reasonable notice period, he was not “actively” employed and so did not qualify under the terms of the plan.

[51] The employee’s appeal was allowed. The Ontario Court of Appeal relied principally on its prior decision in *Taggart v. Canada Life Assurance Co.* (2006), 50 C.C.P.B. 163, concerning a similar question related to pension benefits. In that case, Sharpe J.A. rightly cautioned that courts should not ignore the legal nature of employees’ claims. “The claim is not”, he said, “for the pension benefits themselves. Rather, it is for common law contract damages as compensation for the pension benefits [the employee] would have earned had [the employer] not breached the contract of employment” (para. 16). Consequently, “a terminated employee is entitled to claim damages for the loss of pension benefits that would have accrued had the employee worked until the end of the notice period” (para. 13). With respect to the role of a bonus plan’s contractual terms, Sharpe J.A. explained that “[t]he question at this stage is whether

there is something in the language of the pension contract between the parties that takes away or limits that common law right" (para. 20).

[52] The Court of Appeal in *Paquette* built upon the approach in *Taggart*, proposing that courts should take a two-step approach to these questions. First, courts should "consider the [employee's] common law rights" (para. 30). That is, courts should examine whether, but for the termination, the employee would have been entitled to the bonus during the reasonable notice period. Second, courts should "determine whether there is something in the bonus plan that would specifically remove the [employee's] common law entitlement" (para. 31). "The question", van Rensburg J.A. explained, "is not whether the contract or plan is ambiguous, but whether the wording of the plan unambiguously alters or removes the [employee's] common law rights" (para. 31).

[53] I agree with van Rensburg J.A. that this is the appropriate approach. It accords with basic principles of damages for constructive dismissal, anchoring the analysis around reasonable notice. As the court recognized in *Taggart*, and reiterated in *Paquette*, when employees sue for damages for constructive dismissal, they are claiming for damages as compensation for the income, benefits, and bonuses they would have received had the employer not breached the implied term to provide reasonable notice (see also *Iacobucci v. WIC Radio Ltd.*, 1999 BCCA 753, 72 B.C.L.R. (3d) 234, at paras. 19 and 24; *Gillies v. Goldman Sachs Canada Inc.*, 2001 BCCA 683, 95 B.C.L.R. (3d) 260, at paras. 10-12 and 25; *Keays*, at paras. 54-55). Proceeding directly to an examination of contractual terms divorces the question of damages from the underlying breach, which is an error in principle.

[54] Moreover, the approach in *Paquette* respects the well-established understanding that the contract effectively "remains alive" for the purposes of assessing the employee's damages, in order to determine what compensation the employee would have been entitled to

> but for the dismissal (see, e.g., *Nygard Int. Ltd. v. Robinson* (1990), 46 B.C.L.R. (2d) 103 (C.A.), at pp. 106-7, per Southin J.A., concurring; *Gillies*, at para. 17).
>
> [55] Courts should accordingly ask two questions when determining whether the appropriate quantum of damages for breach of the implied term to provide reasonable notice includes bonus payments and certain other benefits. Would the employee have been entitled to the bonus or benefit as part of their compensation during the reasonable notice period? If so, do the terms of the employment contract or bonus plan unambiguously take away or limit that common law right?

[50] In my view, the key point made by the Supreme Court about the first stage of the two-step test is that the purpose is to recognize that the contract of employment is treated as alive and continuing to subsist during the notice period, so that the question is, what would the employee have earned or been entitled to receive had their employment not been wrongfully terminated?

[51] Mr. Matthews argued that since the sale of the company took place during the 15-month reasonable notice period, he was *prima facie* entitled to common law damages for the lost LTIP payment. Ocean's position was that Mr. Matthews could not satisfy the first stage of the two-part test. Mr. Matthews had a common law entitlement to damages only "for all compensation and benefits that are integral to his compensation," and the LTIP was not integral because he did not have a vested right at the date of termination.

[52] The Supreme Court rejected Ocean's position. It agreed that "whether a bonus or benefit is 'integral' to the employee's compensation assists in answering

the question of what the employee would have been paid during the reasonable notice period": at para. 58. However, in Mr. Matthews' case, there was no need to ask whether the benefit was an integral part of his compensation because there was no question that, had he remained employed during the notice period, he would have received the LTIP benefit. It was not a discretionary payment, and he would have been entitled to it. Therefore, he was *prima facie* entitled to receive damages as compensation for the LTIP. The only issue for the Supreme Court to resolve was whether the terms of the LTIP unambiguously limited or removed Mr. Matthews' common law right to receive damages.

[53] Turning to that issue, the Supreme Court examined the terms of the LTIP to see if there were any that removed Mr. Matthews' common law entitlement. It concluded that the limiting terms did not have that effect. The two relevant clauses provided:

> 2.03 CONDITIONS PRECEDENT:
>
> [Ocean] shall have no obligation under this Agreement to the Employee unless on the date of a Realization Event the Employee is a full-time employee of [Ocean]. For greater certainty, this Agreement shall be of no force and effect if the employee ceases to be an employee of [Ocean], regardless of whether the Employee resigns or is terminated, with or without cause.
>
> 2.05 GENERAL:
>
> The Long Term Value Creation Bonus Plan does not have any current or future value other than on the date of a Realization Event and shall not be calculated as part of

> the Employee's compensation for any purpose, including in connection with the Employee's resignation or in any severance calculation.

[54] The Supreme Court emphasized, at paras. 64-65, that the wording of the LTIP must "unambiguously limit[] or remove[] the employee's common law right", and that the provisions "must be absolutely clear". To that end, language requiring an employee to be "full-time," like in clause 2.03, would not suffice to remove an employee's common law right to damages. Had Mr. Matthews been given proper notice, he would have been a full-time employee during the notice period.

[55] The Supreme Court also noted, at para. 66, that "where a clause purports to remove an employee's common law right to damages upon termination 'with or without cause', such as clause 2.03, this language will not suffice," pointing out that termination without cause does not mean termination without notice. And in any event, because an employment contract is not treated as terminated until after the reasonable notice period expires for the purpose of calculating damages for wrongful dismissal, even if the clauses had expressly referred to wrongful termination, that would not have been sufficient to unambiguously alter the employee's common law entitlement.

[56] In the result, the Supreme Court concluded that under step one, Mr. Matthews was *prima facie* entitled to the LTIP payment as part of his compensation, and under step two, the terms of the LTIP did not unambiguously remove that entitlement.

C. ANALYSIS

[57] Based on the Supreme Court's approach and analysis in *Matthews*, which follows *Lin*, *Paquette*, and *Taggart*, in my view, had the trial judge had the benefit of the *Matthews* decision and had he applied that decision as the legal framework for analyzing the appellant's claim, his analysis and conclusion would not have changed. And it of course follows that there would be no basis to interfere with the trial judge's decision on appeal. I base this conclusion on paras. 38-48 of the trial judge's reasons:

> [38] Benefit Plans generally include limitations or conditions on payments out of the plan. Where an employee has been dismissed without cause, it may be argued that the terms of such Benefit Plans limit or eliminate the employee's entitlements upon the termination of his or her employment. In *Taggart v. Canada Life Assurance Co.*, Sharpe J.A. explained the correct approach for analysing such issues. The first step in the analysis is to determine the employee's common law right to damages for breach of contract. The second step is to determine whether the terms of the relevant Benefit Plan alter or remove a common-law right. Moreover, clear language is required to limit common law entitlements.
>
> [39] Applying this analysis to the CIP, in my view it is clear that the CIP represented an integral part of Manastersky's compensation. His participation in the CIP was included in his Contract of Employment and he continued to participate in the Plan throughout his 13 years of employment at RBC. Although the allocation of a specific number of Points to participants was discretionary, once awarded, Points could not be reduced without the agreement of the participant. Manastersky's Points allocation had remained constant

since 2007, when he was awarded 50% of the total available Points under the Plan. Because the entitlements under the Plan depended on investment earnings from the Mezzanine Fund, the amounts earned by participants would fluctuate from year to year. However the calculation of a participant's share of investment proceeds was nondiscretionary in the sense that it would be determined through the application of the Payment Formula set out in the Plan itself. Over the course of Manastersky's 13 years at RBC, his average share of investment proceeds per investment year was approximately $635,000, representing well over 50% of his total annual income.

[40] I note that in *Bain v. UBS Securities Canada Inc.*, D.A. Wilson J. set out a general test for determining whether a bonus is integral to the employee's compensation. One element of the test was whether the bonus was received each year, although in different amounts. It might be noted that in this case no payments had been made from the CIP since 2007, since the Fund 2 investment period that had commenced in 2006 had not yet concluded. Nevertheless, participants in the CIP continued to accumulate entitlements each year. The fact that no actual payments had been made out of the Plan since 2007 does not alter or diminish the significance and materiality of the Plan to a participant's annual compensation.

[41] In short, the CIP was a significant, nondiscretionary variable form of compensation that represented more than half of Manastersky's annual income, similar to the variable forms of incentive compensation considered by Corbett J. in *Lin v. Ontario Teachers' Pension Plan Board*. It was integral to his compensation and therefore forms part of his presumptive entitlement to damages at common law during the notice period.

[42] The second stage of the analysis is to consider whether there are any provisions in the CIP which limit or eliminate this presumptive entitlement upon termination of employment. The CIP did make provision for the

impact of a termination of employment on an employee's entitlements under the Plan. However, far from eliminating or limiting Manastersky's entitlements upon termination, the CIP provided that all of Manastersky's outstanding Points would immediately vest in the event that he was terminated without cause. It was for this reason that the Termination Offer provided that, despite the termination of his employment, Manastersky's rights under the CIP remained fully vested. In short, the CIP did not purport to limit or reduce Manastersky's entitlements under the Plan in the event that his employment was terminated without cause.

[43] RBC argued that Manastersky was not entitled to compensation in respect of the CIP during the common law notice period by virtue of a provision which allowed RBC to "terminate the Plan effective as of the end of any Investment Period with respect to future Investment Periods." As noted earlier, by the fall 2013, the CIP was nearing the end of the investment period for Fund 2, by virtue of the fact that the total amount invested through the Mezzanine Fund was approaching $160 million. Upon the conclusion of the Fund 2 investment period, a new investment period would automatically begin. However, RBC could also elect to terminate the CIP with respect to future investment periods upon the conclusion of the Fund 2 investment period and prior to the commencement of Fund 3. In fact, RBC exercised this right on June 25, 2014, when it terminated the CIP in respect of future investment periods.

[44] I do not believe that the fact that RBC had the option of terminating the Plan at the end of an investment period should be regarded as limiting Manastersky's entitlement to notice at common law. First, RBC's right to terminate the CIP was in no way tied to the termination of Manastersky's employment. Far from containing "clear language" limiting rights upon termination of employment, the provision in the CIP permitting RBC to terminate the Plan did not purport to limit or reduce his common law entitlements. Nor could it be said that the parties did not turn their minds to the consequences

flowing from the termination of Manastersky's employment on his entitlements under the CIP. In fact, the CIP enhanced Manastersky's entitlements in the event his employment was terminated without cause, through accelerated vesting of his Points.

[45] Further, the fact that RBC terminated the CIP in respect of future investment periods on June 25, 2014, four months after Manastersky's dismissal without cause, does not alter this analysis. As Sharpe JA explained in *Taggart*, in cases where a terminated employee seeks compensation for entitlements under a benefit plan, the claim is not for the benefits themselves. Rather, the claim is for common law contract damages as compensation for the benefits that the employee would have earned had the employer not breached the contract of employment. The employee is claiming for the lost opportunity to continue to earn or receive benefits that would have been available in the event their employment had continued. As of the date of the Termination Offer, RBC had not in fact terminated the CIP, and it therefore remained in place as an integral component of Manastersky's compensation.

[46] What if Manastersky's employment had continued past February 14, 2014 and in June 2014 RBC had terminated the CIP without offering Manastersky some alternate, comparable form of compensation? Although consistent with the terms of the CIP, this would have amounted to a unilateral significant reduction in his compensation, as it would have eliminated the opportunity for him to continue to accrue entitlements through the CIP. This would in all likelihood have amounted to a constructive dismissal, thereby triggering an entitlement to damages at common-law, including damages for the lost opportunity to continue to earn entitlements under the CIP.

[47] In any event, RBC had not in fact terminated the CIP as of the date of Manastersky's termination of employment. Nothing in the CIP purported to limit or restrict his entitlements under the Plan upon the

> termination of his employment. His termination without cause deprived him of the opportunity to continue to earn entitlements under the CIP and he is entitled to be compensated in damages for that lost opportunity.
>
> [48] RBC also argues that rather than terminate the CIP, it could simply have elected to cease making any additional investments in the Mezzanine Fund, effectively eliminating Manastersky's opportunity to earn additional entitlements under the CIP. But if RBC could not directly reduce Manastersky's compensation unilaterally, it could not achieve the same result through indirect means. To be sure, RBC was perfectly entitled to make investment decisions as to how and where it wished to invest its capital but, in doing so, it could not escape its contractual and common law obligations to Manastersky. [Footnotes omitted.]

[58] The trial judge applied all of the principles from *Matthews*. He applied the two-step test by first determining the appellant's common law right to damages for breach of contract, and second determining whether the CIP altered or removed the appellant's common law right. And he took note that clear language is required to limit common law entitlements.

[59] At the first step, to determine the appellant's common law right to damages, he addressed the question whether the CIP represented an integral part of the appellant's compensation, focusing on the evidence of the significance and materiality of the CIP to the appellant's annual compensation, regardless of whether it was paid or just accrued annually.

[60] At the second step, the trial judge found that the terms of the CIP provided for full vesting on termination without cause, and did not purport to reduce the

appellant's entitlement upon the termination of his employment. He considered the effect of the provisions that allowed the respondent to terminate the CIP for future investments, which it ultimately did during the notice period. However, interpreting those provisions, as he was entitled to do (*Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633), the trial judge found that the respondent's option to terminate the CIP did not limit the appellant's entitlement to notice at common law. He also specifically rejected the respondent's argument that because it could terminate the CIP by simply ceasing to make additional investments into the Fund, it was entitled to thereby reduce the appellant's compensation by eliminating his opportunity to earn his entitlements under the CIP. The trial judge concluded that the respondent's freedom to make investment decisions did not allow it to "escape its contractual and common law obligations".

[61] In his analysis of the terms of the CIP, the trial judge addressed their effect on termination under step two, as well as their effect on the appellant's common law entitlement under step one. In fact, as my colleague observes, at para. 21, the twist in this case is that the court was required to determine whether the terms of the CIP limited the appellant's common law entitlement. The trial judge addressed this issue directly by interpreting the terms of the CIP in the context of the factual record.

[62] The determination at step one as to whether the CIP constituted an integral part of the appellant's compensation package was the key issue before the court

at trial and on appeal.[3] While it is acknowledged that the CIP was not discretionary, the question whether it formed an integral component of the appellant's compensation arose because the respondent took the position that it was entitled to discontinue the CIP (which it did during the notice period) without replacing it with a comparable benefit. My colleague accepts the respondent's position that Mr. Manastersky's entitlement was fund-specific, and that the appellant did not have any further right to claim common law damages once the Fund was wound up and he received the value of his vested interest in the CIP. However, whether the appellant's entitlement was "fund-specific" was the question before the court. Under step one, the issue was whether the appellant was entitled to receive an equivalent benefit once the fund was wound up, because the CIP benefit formed an integral part of his compensation.

[63] My colleague says that the appellant was only entitled to the CIP and that he got what he was entitled to. He relies on the fact that the respondent was not obliged to start a third Fund.

[64] The appellant does not dispute the respondent's entitlement to make business decisions, including whether to continue with the Mezzanine Fund or the

[3] My colleague comments, at para. 12, of his reasons that counsel for the appellant in oral submissions agreed that because the CIP was not discretionary, the issue of whether the CIP was integral did not arise. As I understand her comment in the context of her full submissions, she agreed that because the CIP was not discretionary, it was unnecessary to consider whether it was integral on that basis. However, the issue in the case remains whether the employer could cancel the CIP without replacing it or giving reasonable notice, and that turns on whether it was integral to the appellant's compensation package.

CIP. However, that does not determine his entitlement to be compensated at the level reflected by his participation in the Fund through the CIP. That turns on whether the CIP formed an integral part of his compensation package. The trial judge found at step one that it did, in the paragraphs quoted above. I agree with his analysis.

[65] Furthermore, the terms of the CIP do not undermine the conclusion that it formed an integral part of the appellant's compensation. There are no terms in the CIP or in the appellant's employment agreement that unambiguously state that if the respondent decided to terminate the CIP, the effect would be to discontinue the employee's right to receive compensation at a level based on the performance of the Fund. The trial judge found that there was no unambiguous language that would affect the appellant's common law entitlement. I agree with that finding as well.

[66] While the Supreme Court in *Matthews* endorsed the requirement for unambiguous language in order to disentitle an employee at stage two, it follows that the same requirement applies at stage one. In endorsing the requirement, the Supreme Court referred to the principle of contractual interpretation for unilateral contracts that clauses excluding or limiting liability be strictly construed. It stated, at paras. 64-65, that the principle "applies with particular force", and added that "the provisions of the agreement must be absolutely clear and unambiguous."

There is no basis to suggest that the court intended to limit this requirement to the stage two portion of the analysis.

[67] The appellant was hired to be a director of the Mezzanine Fund and to be compensated in significant part based on the performance of the Fund through the CIP. Eventually the respondent decided to bring the Fund in-house and to eliminate the CIP incentive performance plan. The respondent was certainly entitled to do that as a business decision. However, the result was to effectively eliminate the appellant's position with the respondent as the director of the Fund. When the respondent decided to make that decision, it was obliged to give the appellant reasonable notice, and to pay him what he would have earned during that period or to offer him a comparable position at a comparable rate of compensation. Failure to do so would constitute constructive dismissal: *Farber v. Royal Trust*, [1997] 1 SCR 846, at paras. 33-36. When it became clear that there would be no comparable position, the respondent terminated the appellant's employment, whereupon he was entitled to be paid what he would have earned had he remained employed during the reasonable notice period.

[68] Although the respondent's Mezzanine CIP was a complex, high-end financial vehicle, as was the appellant's very remunerative entitlement to his points allocation in it, the law with respect to the two-step process for determining entitlement to damages in lieu of notice for wrongful termination of employment, set out by the Supreme Court in *Matthews*, applies to it in the same way as it does

to a more simple bonus or benefit. The court asks first, what is the employee's common law entitlement during the notice period, and second, whether the terms of the employment contract or bonus plan "unambiguously take away or limit that common law right" on termination.

[69] In this case, there is no language that purports to reduce the appellant's compensation if the CIP is discontinued (step one), or to limit the appellant's entitlement because of his dismissal (step two). The language that my colleague focuses on is the right of the respondent to discontinue the plan. That right is merely the right of any business to make business decisions in its own interest. It is not an unambiguous right to also reduce the appellant's compensation, either while he remains employed or is in the reasonable notice period following the termination of his employment.

[70] What the Supreme Court's decision in *Matthews* emphasized, at para. 65, is how "absolutely clear and unambiguous" the provisions of the employment agreement must be "to remove an employee's common law right to damages." There is no language in the appellant's employment agreement stating that if the CIP is terminated, so also is his entitlement to be compensated at the same level.

[71] In my view, the trial judge was correct in his analysis of the CIP, and in his application of the law as it was then and as confirmed in *Matthews*. The trial judge's decision remains entitled to the deference of this court.

[72] I would affirm my original decision to dismiss the appeal from the trial judge's decision, with costs.

Released: June 24, 2021 "K. F."

"K. Feldman J.A."

TAB 7

David Matthews *Appellant*

v.

Ocean Nutrition Canada Limited *Respondent*

and

Canadian Association for Non-Organized Employees, Don Valley Community Legal Services, Law Students' Legal Advice Program, Canadian Association of Counsel to Employers and Parkdale Community Legal Services *Interveners*

Indexed as: Matthews *v.* Ocean Nutrition Canada Ltd.

2020 SCC 26

File No.: 38252.

2019: October 8; 2020: October 9.

Present: Wagner C.J. and Moldaver, Côté, Brown, Rowe, Martin and Kasirer JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR NOVA SCOTIA

Employment law — Constructive dismissal — Duty to provide reasonable notice — Damages — Employee working for employer for approximately 14 years — Employer providing long term incentive plan according to which employee would receive bonus payment if company sold — Company sold soon after employee constructively dismissed — Whether damages for breach of duty to provide reasonable notice include incentive bonus.

Beginning in 1997, M, an experienced chemist, occupied several senior management positions with Ocean Nutrition Canada Limited ("Ocean"). As a senior executive, M was part of Ocean's long term incentive plan ("LTIP"), a contractual arrangement designed to reward employees for their previous contributions and to provide

David Matthews *Appelant*

c.

Ocean Nutrition Canada Limited *Intimée*

et

Canadian Association for Non-Organized Employees, Don Valley Community Legal Services, Law Students' Legal Advice Program, Association canadienne des avocats d'employeurs et Parkdale Community Legal Services *Intervenants*

Répertorié : Matthews *c.* Ocean Nutrition Canada Ltd.

2020 CSC 26

N° du greffe : 38252.

2019 : 8 octobre; 2020 : 9 octobre.

Présents : Le juge en chef Wagner et les juges Moldaver, Côté, Brown, Rowe, Martin et Kasirer.

EN APPEL DE LA COUR D'APPEL DE LA NOUVELLE-ÉCOSSE

Droit de l'emploi — Congédiement déguisé — Obligation de donner un préavis raisonnable — Dommages-intérêts — Employé au service de l'employeur pendant environ 14 ans — Régime d'intéressement à long terme créé par l'employeur prévoyant le versement d'une prime à l'employé en cas de vente de l'entreprise — Entreprise vendue peu de temps après le congédiement déguisé de l'employé — Est-ce que les dommages-intérêts accordés à l'égard du manquement à l'obligation de donner un préavis raisonnable doivent inclure la prime d'intéressement?

À partir de 1997, M, un chimiste expérimenté, a occupé plusieurs postes de direction chez Ocean Nutrition Canada Limited (« Ocean »). En tant que cadre supérieur, M participait au régime d'intéressement à long terme (« RILT ») d'Ocean, un arrangement contractuel visant à récompenser les employés pour leurs contributions antérieures au

an incentive to continue contributing to the company's success. Under the LTIP, a "Realization Event", such as the sale of the company, would trigger payments to employees who qualified under the plan. In 2007, Ocean hired a new Chief Operating Officer, who began a campaign to marginalize M in the company, limiting M's responsibilities and lying to M about his status and prospects with Ocean. Despite his problems with senior management, the LTIP was a key reason for which M wanted to stay with Ocean, anticipating Ocean would soon be sold. However, M eventually left Ocean in June 2011, taking a position with a new employer.

About 13 months after M's departure, Ocean was sold for $540 million. The sale constituted a Realization Event for the purposes of the LTIP. Since M was not actively employed on that date, Ocean took the position that M did not satisfy the terms of the plan, and he did not receive a payment. M filed an application against Ocean alleging that he was constructively dismissed, and that the constructive dismissal was carried out in bad faith and in breach of Ocean's duty of good faith. The trial judge concluded that Ocean constructively dismissed M, and that M was owed a reasonable notice period of 15 months. The trial judge also held that M would have been a full-time employee when the Realization Event occurred had he not been constructively dismissed, and that, because the terms of the LTIP did not unambiguously limit or remove his common law right to damages, M was entitled to damages equivalent to what he would have received under the LTIP. The Court of Appeal unanimously upheld the decision that M had been constructively dismissed and that the appropriate reasonable notice period was 15 months. However, a majority of the court found that M was not entitled to damages on account of the lost LTIP payment.

Held: The appeal should be allowed, the judgment of the Court of Appeal set aside and the trial judgment restored.

At common law, an employer has the right to prompt an employee to choose to leave their job in circumstances that amount to a dismissal subject to the duty to provide

succès de l'entreprise et à les inciter à continuer de le faire. Conformément au RILT, un « événement déclencheur », par exemple la vente de l'entreprise, entraînerait le versement des paiements prévus aux employés admissibles aux termes du régime. En 2007, Ocean a embauché un nouveau directeur de l'exploitation, qui a entamé une campagne de marginalisation de M au sein de l'entreprise, en limitant ses responsabilités et en lui mentant au sujet de son statut et de son avenir au sein d'Ocean. Malgré les problèmes que connaissait M avec la haute direction, le RILT était une raison déterminante pour laquelle il voulait continuer de travailler pour Ocean, car il s'attendait à ce que l'entreprise soit bientôt vendue. Cependant, M a finalement quitté Ocean en juin 2011, acceptant un poste chez un nouvel employeur.

Environ 13 mois après le départ de M, Ocean a été vendue pour la somme de 540 millions de dollars. Cette vente constituait, pour les besoins du RILT, l'événement déclencheur. Comme M ne travaillait plus activement pour l'entreprise au moment de la vente, Ocean a soutenu que M ne satisfaisait pas aux conditions du régime, et il n'a pas reçu de prime. M a présenté contre Ocean une requête dans laquelle il alléguait qu'il avait été congédié de façon déguisée, et que ce congédiement avait été effectué de mauvaise foi et en contravention à l'obligation d'Ocean d'agir de bonne foi. Le juge de première instance a conclu qu'Ocean avait congédié M de manière déguisée et que ce dernier avait droit à un préavis raisonnable de 15 mois. Le juge de première instance a également conclu que M aurait été un employé à temps plein de l'entreprise lorsque l'événement déclencheur s'est produit s'il n'avait pas fait l'objet d'un congédiement déguisé, et que, comme les modalités du RILT n'avaient pas pour effet de limiter ou de supprimer clairement son droit à des dommages-intérêts en vertu de la common law, M avait droit à des dommages-intérêts d'un montant équivalant au paiement qu'il aurait reçu en vertu du RILT. La Cour d'appel a confirmé à l'unanimité la décision portant que M avait fait l'objet d'un congédiement déguisé et que le préavis raisonnable approprié était de 15 mois. Toutefois, les juges majoritaires de la Cour d'appel ont conclu que M n'avait pas droit à des dommages-intérêts pour la perte du paiement prévu par le RILT.

Arrêt : Le pourvoi est accueilli, l'arrêt de la Cour d'appel est écarté et le jugement de première instance est rétabli.

Suivant la common law, un employeur a le droit de pousser un employé à quitter son emploi dans des circonstances qui équivalent à un congédiement, pourvu

reasonable notice. The obligation to provide reasonable notice does not, in theory, turn on the presence or absence of good faith. The contractual breach that arises from the employer's choice is simply the failure to provide reasonable notice, which leads to an award of damages in lieu thereof. A breach of the duty to exercise good faith in the manner of dismissal is a distinct contractual breach and is independent of any failure to provide reasonable notice. It can serve as a basis to answer for foreseeable injury that results from callous or insensitive conduct in the manner of dismissal. Damages arising out of the same dismissal are calculated differently depending on the breach invoked. The nature of the contractual breach of good faith is of a different order than that associated with the failure to provide reasonable notice.

Courts should ask two questions when determining whether the appropriate quantum of damages for breach of an implied term to provide reasonable notice includes bonus payments. First, courts should consider the employee's common law rights and examine whether, but for the termination, the employee would have been entitled to the bonus or benefit as part of their compensation during the reasonable notice period. Second, if so, courts should determine whether the terms of the employment contract or bonus plan unambiguously take away or limit that common law right. This approach accords with basic principles of damages for constructive dismissal, anchoring the analysis around reasonable notice. When an employee sues for damages for constructive dismissal, they are claiming for damages as compensation for the income, benefits, and bonuses they would have received had the employer not breached the implied term to provide reasonable notice. This approach respects the well-established understanding that the contract effectively remains alive for the purposes of assessing the employee's damages, in order to determine what compensation the employee would have been entitled to but for the dismissal. Damages for wrongful dismissal are designed to compensate the employee for the breach by the employer of the implied term in the employment contract to provide reasonable notice of termination. There is no such implied term of the contract to provide payment in lieu. The payment in lieu is not damages for a breach of the contract, but rather one component of the compensation provided for in the contract. If an employer

que cet employeur s'acquitte de son obligation de donner un préavis raisonnable. L'obligation de donner un préavis raisonnable ne dépend pas, en théorie, de la question de savoir s'il y a eu ou non bonne foi. Le manquement au contrat découlant de la décision de l'employeur est simplement le défaut de donner un préavis raisonnable, situation qui entraîne le paiement de dommages-intérêts tenant lieu de préavis. Un manquement à l'obligation d'agir de bonne foi dans la façon de congédier l'employé constitue une violation contractuelle distincte et est indépendant de tout manquement à l'obligation de donner un préavis raisonnable. Il peut servir de fondement permettant d'exiger réparation à l'égard d'un préjudice prévisible résultant d'un traitement brutal ou implacable de la part de l'employeur dans la façon dont il a congédié l'employé. Les dommages-intérêts découlant d'un même congédiement sont calculés différemment selon la violation reprochée. La nature du manquement à l'obligation contractuelle d'agir de bonne foi n'est pas du même ordre que dans le cas du défaut de donner un préavis raisonnable.

Les tribunaux devraient se poser deux questions lorsqu'ils sont appelés à décider si le montant des dommages-intérêts qu'il convient d'accorder pour manquement à l'obligation tacite de donner un préavis raisonnable doit inclure les primes. Premièrement, les tribunaux devraient considérer les droits dont dispose l'employé en vertu de la common law et se demander si, n'eût été son congédiement, l'employé aurait eu droit à la prime ou à l'avantage dans le cadre de ses conditions de rémunération pendant la période de préavis raisonnable. Deuxièmement, dans l'affirmative, les tribunaux devraient déterminer si les modalités du contrat de travail ou du régime de primes ont pour effet de supprimer ou de limiter clairement ce droit que confère la common law. Cette démarche est conforme aux principes fondamentaux applicables aux dommages-intérêts pour congédiement déguisé, l'analyse s'attachant à la question du préavis raisonnable. Lorsqu'un employé intente une action en dommages-intérêts pour congédiement déguisé, il sollicite des dommages-intérêts à titre de dédommagement pour le revenu, les prestations et les primes qu'il aurait touchés si l'employeur n'avait pas manqué à son obligation tacite de donner un préavis raisonnable. Cette démarche est compatible avec l'interprétation bien établie selon laquelle le contrat demeure effectivement en vigueur pour les besoins de l'évaluation du préjudice de l'employé en vue de calculer le montant de l'indemnité à laquelle ce dernier aurait eu droit n'eût été son congédiement. Les dommages-intérêts versés pour congédiement injustifié visent à indemniser l'employé à

fails to give proper notice or pay in lieu, the breach is in the failure to pay, not in the termination.

In the present case, in determining whether M's damages include an amount to compensate him for his lost LTIP payment, the focus should be on what damages were appropriately due for Ocean's failure to provide M with reasonable notice and not on whether the terms of the LTIP were plain and unambiguous. The issue is not whether M is entitled to the LTIP in itself, but rather what damages he is entitled to and, specifically, whether he was entitled to compensation for bonuses he would have earned had Ocean not breached the employment contract. It is uncontested that the Realization Event occurred during the notice period and therefore, but for M's dismissal, he would have received an LTIP payment during that period. In such circumstances, there is no need to ask whether the LTIP payment was integral to his compensation. On the first question, M is prima facie entitled to receive damages as compensation for the lost bonus. On the second question, the LTIP does not unambiguously limit or remove M's common law right. Had M been given proper notice, he would have been full-time or actively employed throughout the reasonable notice period. For the purpose of calculating wrongful dismissal damages, the employment contract is not treated as terminated until after the reasonable notice period expires. M should therefore be awarded the amount of the LTIP as part of his common law damages for breach of the implied term to provide reasonable notice. On the issue of good faith, it suffices to say that a contractual breach of good faith rests on a wholly distinct basis from that relating to the failure to provide reasonable notice.

l'égard de la violation par l'employeur de la condition implicite du contrat d'emploi selon laquelle ce dernier doit donner à l'employé un préavis raisonnable de cessation d'emploi. Le contrat ne comporte aucune condition implicite portant que l'employeur doit verser une indemnité tenant lieu de préavis. L'indemnité tenant lieu de préavis raisonnable ne constitue pas des dommages-intérêts pour violation du contrat, mais plutôt une portion de l'indemnité prévue au contrat. Si un employeur ne donne pas un préavis adéquat ou une indemnité en tenant lieu, la violation réside dans le non-paiement d'une indemnité et non dans le congédiement.

En l'espèce, afin de déterminer si les dommages-intérêts accordés à M doivent inclure une somme l'indemnisant pour la perte du paiement prévu par le RILT, il faut mettre l'accent sur le montant des dommages-intérêts qu'il convenait d'accorder à M parce qu'Ocean ne lui a pas donné un préavis raisonnable, et non sur la question de savoir si les modalités du RILT étaient claires et non ambiguës. Il ne s'agit pas de décider si M est admissible au RILT, mais plutôt de déterminer le montant des dommages-intérêts auquel il a droit et, plus précisément, s'il a droit d'être indemnisé pour les primes qu'il aurait touchées si Ocean n'avait pas contrevenu au contrat de travail. Il n'est pas contesté que l'événement déclencheur s'est produit pendant la période de préavis et que, par conséquent, n'eût été son congédiement, M aurait reçu le paiement prévu par le RILT durant cette période. Dans ces circonstances, il est inutile de se demander si ce paiement faisait partie intégrante de sa rémunération. En ce qui concerne la première question, M a droit, à première vue, de recevoir des dommages-intérêts à titre de dédommagement pour la prime qu'il a perdue. En ce qui a trait à la deuxième question, le RILT n'a pas pour effet de limiter ou de supprimer clairement le droit que confère la common law à M. Si un préavis adéquat avait été donné à M, ce dernier aurait été un employé à temps plein ou un employé actif de l'entreprise pendant la période de préavis raisonnable. Pour les besoins du calcul du montant des dommages-intérêts à verser en cas de congédiement injustifié, le contrat de travail est considéré comme étant résilié uniquement après l'expiration de la période de préavis raisonnable. Par conséquent, le montant de la prime prévue par le RILT doit être inclus dans les dommages-intérêts accordés à M, en vertu de la common law, pour le manquement à l'obligation tacite de lui donner un préavis raisonnable. Relativement à la question de bonne foi, qu'il suffise de dire qu'un manquement à l'obligation contractuelle d'agir de bonne foi repose sur des fondements entièrement distincts de ceux liés à l'omission de donner un préavis raisonnable.

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Statutes and Regulations Cited

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Howard Levitt, *Allyson Lee*, *Blair Mitchell* and *Saba Khan*, for the appellant.

Nancy F. Barteaux, *Q.C.*, *Mary B. Rolf* and *Kate E. Ross*, for the respondent.

Stacey Reginald Ball, *Nadine Côté* and *Sean O'Donnell*, for the intervener the Canadian Association for Non-Organized Employees.

Andrew Monkhouse and *Alexandra Monkhouse*, for the intervener Don Valley Community Legal Services.

Martin Sheard and *David McWhinnie*, for the intervener the Law Students' Legal Advice Program.

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POURVOI contre un arrêt de la Cour d'appel de la Nouvelle-Écosse (les juges Farrar, Bryson et Scanlan), 2018 NSCA 44, 2018 C.L.L.C. ¶210-053, 48 C.C.E.L. (4th) 171, [2018] N.S.J. No. 200 (QL), 2018 CarswellNS 393 (WL Can.), qui a écarté en partie une décision du juge LeBlanc, 2017 NSSC 16, [2017] N.S.J. No. 32 (QL), 2017 CarswellNS 55 (WL Can.), avec motifs supplémentaires, 2017 NSSC 123, [2017] N.S.J. No. 161 (QL), 2017 CarswellNS 325 (WL Can.). Pourvoi accueilli.

Howard Levitt, *Allyson Lee*, *Blair Mitchell* et *Saba Khan*, pour l'appelant.

Nancy F. Barteaux, *c.r.*, *Mary B. Rolf* et *Kate E. Ross*, pour l'intimée.

Stacey Reginald Ball, *Nadine Côté* et *Sean O'Donnell*, pour l'intervenante Canadian Association for Non-Organized Employees.

Andrew Monkhouse et *Alexandra Monkhouse*, pour l'intervenant Don Valley Community Legal Services.

Martin Sheard et *David McWhinnie*, pour l'intervenant Law Students' Legal Advice Program.

Tim Lawson, *Brandon Kain* and *Adam Goldenberg*, for the intervener the Canadian Association of Counsel to Employers.

Christopher Rootham, *Andrew Montague-Reinholdt* and *John No*, for the intervener Parkdale Community Legal Services.

The judgment of the Court was delivered by

Kasirer J. —

I. Overview

[1] This appeal bears on the redress available to an employee who, by reason of the circumstances of his departure from a job he had held for many years, is treated in law as if he were dismissed. By extension, it concerns some of the proper contours of an employer's common law right to determine the composition of its workforce.

[2] Different complaints are often made by employees who sue for wrongful dismissal. This case is no exception: in his original application, the employee alleged he was dismissed "without notice" and that this dismissal was in breach of the employer's "duty of good faith". He asked for damages reflecting his entitlement to reasonable notice, including an incentive bonus that fell due during the period, as well as damages for the employer's dishonest conduct, including punitive damages and damages in the amount of the lost bonus should it be excluded by a contractual term.

[3] The fact that the employee was constructively dismissed and is entitled to notice is no longer in dispute. The parties continue to disagree, however, as to the remedies that should be afforded to the employee at common law. Specifically, the parties dispute whether the failure to provide damages

Tim Lawson, *Brandon Kain* et *Adam Goldenberg*, pour l'intervenante l'Association canadienne des avocats d'employeurs.

Christopher Rootham, *Andrew Montague-Reinholdt* et *John No*, pour l'intervenant Parkdale Community Legal Services.

Version française du jugement de la Cour rendu par

Le juge Kasirer —

I. Aperçu

[1] Le présent pourvoi porte sur les voies de recours qui s'offrent à un employé qui, en raison des circonstances de son départ d'un emploi qu'il a occupé pendant de nombreuses années, est considéré par le droit comme ayant été congédié. Par extension, le pourvoi porte également sur les paramètres applicables au droit des employeurs de déterminer la composition de leurs effectifs en common law.

[2] Divers griefs sont souvent soulevés lorsqu'un employé intente une action pour congédiement injustifié. La présente affaire ne fait pas exception : dans sa demande initiale, l'employé alléguait qu'il avait été congédié [traduction] « sans préavis » et que ce congédiement constituait un manquement à l'« obligation d'agir de bonne foi » qui incombait à son employeur. Il sollicitait des dommages-intérêts reflétant son droit à un délai de préavis raisonnable, y compris une prime d'intéressement devenue exigible pendant ce délai. Il demandait aussi des dommages-intérêts en raison de la conduite malhonnête de son employeur, y compris des dommages-intérêts punitifs et des dommages-intérêts correspondant à la prime qu'il perdrait si celle-ci était exclue par application d'une disposition contractuelle.

[3] Le fait que l'employé concerné a fait l'objet d'un congédiement déguisé et a droit à un préavis n'est plus en litige. Les parties continuent toutefois d'être en désaccord en ce qui concerne les réparations qui devraient lui être accordées en vertu de la common law. Plus précisément, les parties ne s'entendent

for reasonable notice includes the disputed bonus. Moreover, they are at odds as to the existence of the employer's alleged dishonest conduct and its eventual impact. The employee points this Court to the duty to act honestly in the performance of the contract, which, as this Court has recalled, "was a key component of the good faith requirements which have been recognized in relation to termination of employment contracts" (*Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494, at para. 73, referencing *Wallace v. United Grain Growers Ltd.*, [1997] 3 S.C.R. 701, at para. 98; *Honda Canada Inc. v. Keays*, 2008 SCC 39, [2008] 2 S.C.R. 362, at para. 58).

[4] The parties' disagreement provides an occasion to clarify the duty to provide reasonable notice and to state clearly that a violation of a duty of good faith is a distinct contractual breach, with each alleged breach reflecting different considerations in respect of an employer's common law right of dismissal without cause in employment contracts having an indeterminate term. In making their respective cases, the employee and employer in this case call for significant changes to the law — respectively for an extension of good faith and a narrowing of the duty to provide reasonable notice — changes that, if existing principles are properly understood, are ultimately unnecessary to the disposition of the appeal.

[5] While I see the law as largely settled for the purpose of answering the employee's claim, the manner in which these complaints have been conflated in this case invites the Court to state plainly the different character of these paths of redress for breach of contract in employment. As in this instance, the complaints are sometimes intertwined at the expense of a proper understanding of the law of wrongful dismissal. In fairness to the parties here, this confusion is not altogether uncommon, since courts — even

pas sur la question de savoir si les dommages-intérêts tenant lieu de préavis raisonnable devraient inclure la prime litigieuse. Elles sont également en désaccord quant à l'existence de la conduite malhonnête reprochée à l'employeur et aux répercussions éventuelles de celle-ci. L'employé attire l'attention de notre Cour sur l'obligation qu'ont les parties à un contrat d'agir avec honnêteté dans l'exécution de celui-ci, obligation qui, comme notre Cour l'a rappelé, « constitu[e] un élément clef des exigences de bonne foi qui ont été reconnues en lien avec la résiliation des contrats de travail » (*Bhasin c. Hrynew*, 2014 CSC 71, [2014] 3 R.C.S. 494, par. 73, se référant à *Wallace c. United Grain Growers Ltd.*, [1997] 3 R.C.S. 701, par. 98; *Honda Canada Inc. c. Keays*, 2008 CSC 39, [2008] 2 R.C.S. 362, par. 58).

[4] Ce désaccord donne à la Cour l'occasion d'apporter des précisions sur l'obligation de donner un préavis raisonnable et d'énoncer clairement que la violation d'une obligation d'agir de bonne foi constitue une violation contractuelle distincte, l'un et l'autre de ces manquements soulevant des considérations différentes en ce qui a trait au droit dont dispose un employeur, en vertu de la common law, de congédier sans motif un employé dans le cadre d'un contrat de travail à durée indéterminée. Lors de la présentation de leurs arguments, l'employé et l'employeur en l'espèce ont réclamé des changements importants au droit en la matière — respectivement l'élargissement de l'application de l'obligation d'agir de bonne foi et la restriction de la portée de l'obligation de donner un préavis raisonnable — changements qui, si les principes existants sont interprétés correctement, sont en définitive inutiles pour trancher le pourvoi.

[5] Bien que je considère que le droit applicable pour statuer sur les prétentions de l'employé est dans une large mesure déjà bien établi, la manière dont les griefs soulevés ont été enchevêtrés en l'espèce incite notre Cour à exposer clairement le caractère distinct de ces voies de recours en cas de violations de contrats de travail. Comme c'est le cas dans le présent pourvoi, les griefs sont parfois intimement liés, de telle sorte que les règles de droit applicables au congédiement injustifié ne sont pas interprétées

this Court — have at times conflated them when determining remedies for wrongful dismissal.

[6] For the reasons that follow, as a simple matter of the breach of the duty to provide reasonable notice, I respectfully disagree with the majority of the Court of Appeal's conclusion that the employee's damages do not include the incentive bonus. Given this conclusion, on the employee's own theory of the case, we need not provide a full answer to his allegations of dishonesty; this appeal can be resolved on settled employment law principles, despite the clear dishonest behaviour exhibited by the employer over a protracted period. But beyond clarification as to how courts should analyze claims for financial redress upon dismissal, the employee's complaint that he was mistreated nevertheless deserves some modest comments. In his notice of application, the employee sought a declaration that his termination was wrongful in that his employer's associated conduct was "oppressive", "unfair", and "carried out in bad faith" (A.R., at pp. 144-45). While he has made no detailed pleading on appeal for his original claim for punitive damages and, surprisingly perhaps, made no specific claim for damages for mental distress when he instituted proceedings that can flow when an employer fails to exercise good faith in the manner of dismissal, he remains insistent that the employer breached its obligations of good faith when he was lied to in the run up to the constructive dismissal.

correctement. En toute justice pour les parties au présent pourvoi, une telle confusion n'est pas rare, puisque des tribunaux — même notre Cour — les ont parfois amalgamés dans la détermination des réparations qu'il convenait d'accorder en cas de congédiement injustifié.

[6] Pour les motifs qui suivent, en ce qui concerne la simple question du manquement à l'obligation de donner un préavis raisonnable, je ne puis, avec égards, souscrire à la conclusion des juges majoritaires de la Cour d'appel selon laquelle les dommages-intérêts accordés à l'employé ne doivent pas inclure la prime d'intéressement. Compte tenu de cette conclusion, au vu de la position de l'employé quant aux événements en cause, il ne nous est pas nécessaire de répondre exhaustivement aux prétentions relatives à la malhonnêteté qu'il a formulées. Le présent pourvoi peut être tranché suivant les principes bien établis du droit de l'emploi, malgré la conduite malhonnête évidente manifestée par l'employeur sur une période prolongée. Toutefois, outre les précisions qui s'imposent quant à la manière dont les tribunaux doivent analyser les demandes de réparations pécuniaires formulées à la suite d'un congédiement, le grief de l'employé reprochant à l'employeur de l'avoir traité incorrectement mérite quelques brefs commentaires. Dans son avis de requête, l'employé sollicitait une déclaration portant que son congédiement était injustifié parce que son employeur avait eu à son endroit une conduite [TRADUCTION] « abusive », « injuste » et « entachée de mauvaise foi » (d.a., p. 144-145). Bien qu'il n'ait présenté aucun argument détaillé en appel à l'égard de sa demande initiale de dommages-intérêts punitifs et, fait surprenant peut-être, qu'il n'ait pas, lorsqu'il a intenté son action, sollicité précisément des dommages-intérêts au titre des souffrances morales susceptibles de découler du défaut d'un employeur d'agir de bonne foi lorsqu'il congédie un employé, il continuer d'affirmer avec insistance que son employeur a manqué à son obligation d'agir de bonne foi lorsqu'il lui a menti durant la période précédant son congédiement déguisé.

[7] Some of this doggedness on appeal is explained by the fact that the employee asked not just for money but also sued his employer for non-financial reasons. The trial judge explicitly noted that the employee's sense of self-worth was particularly tied up in his job. This Court has been resolute in asserting that employment is a source of personal fulfilment — that brand of human dignity that comes from work — and this often comes into sharpest focus when a job is unfairly taken away (see, e.g., *Machtinger v. HOJ Industries Ltd.*, [1992] 1 S.C.R. 986, at p. 991). Recently in *Potter v. New Brunswick Legal Aid Services Commission*, 2015 SCC 10, [2015] 1 S.C.R. 500, at para. 84, my colleague Wagner J., prior to his appointment as Chief Justice, identified these considerations as rooted in the "non-monetary benefit all workers may in fact derive from the performance of their work".

[8] Some comment on this aspect of the employee's claim is in my view appropriate. Recognition that an employer has acted dishonestly, independent of any failure to provide notice or other financial loss, can vindicate an employee whose sense of dignity is unfairly shaken when a valued job is lost.

II. Background

[9] David Matthews, an experienced chemist, is one of a handful of individuals in the world with the skills needed to run a large-scale omega-3 facility. Beginning in 1997, Mr. Matthews occupied several senior management positions with Ocean Nutrition Canada Limited ("Ocean"). His expertise proved extremely valuable to the success of Ocean in the manufacture of omega-3 products. Sometime company President and Chief Executive Officer, Robert Orr, testified that "[e]veryone who has gotten any value created out of Ocean in large part owes that in

[7] La persistance avec laquelle l'employé est revenu sur ce point en appel s'explique en partie par le fait qu'il ne poursuit pas son employeur uniquement pour être indemnisé financièrement, mais également pour des raisons non financières. Le juge de première instance a expressément fait remarquer que l'estime de soi de l'employé était particulièrement liée à son travail. Notre Cour a déclaré sans ambages que l'emploi constitue pour les gens une source d'épanouissement personnel — à savoir cette forme de dignité humaine qui découle du travail — et que ce phénomène se manifeste souvent avec encore plus d'acuité lorsqu'une personne perd injustement son emploi (voir, p. ex., *Machtinger c. HOJ Industries Ltd.*, [1992] 1 R.C.S. 986, p. 991). Récemment, dans l'arrêt *Potter c. Commission des services d'aide juridique du Nouveau-Brunswick*, 2015 CSC 10, [2015] 1 R.C.S. 500, par. 84, mon collègue le juge Wagner, avant d'être nommé juge en chef, a indiqué que ces considérations sont enracinées dans « l'avantage non pécuniaire que tout salarié tire de l'exécution de son travail ».

[8] À mon sens, il convient de formuler quelques commentaires à l'égard de cet aspect de l'argumentation de l'employé. Reconnaître qu'un employeur a agi de façon malhonnête, indépendamment de l'existence de toute omission d'accorder un préavis raisonnable ou autre perte financière, peut permettre de restituer à un employé son sens de la dignité, qui a été injustement ébranlé lorsque celui-ci a perdu un emploi qui lui était cher.

II. Contexte

[9] David Matthews, un chimiste expérimenté, est l'une des rares personnes dans le monde qui possèdent les compétences nécessaires pour gérer une installation de fabrication de produits oméga-3 de grande envergure. À partir de 1997, M. Matthews a occupé plusieurs postes de direction chez Ocean Nutrition Canada Limited (« Ocean »). Son expertise s'est avérée extrêmement précieuse à Ocean, lui permettant de connaître du succès dans le domaine de la fabrication de produits oméga-3. L'ancien président-directeur général de l'entreprise, M. Robert

some measure to [Mr. Matthews]" (see 2017 NSSC 16, at para. 66 (CanLII)).

[10] Mr. Matthews was deeply invested in his job. The trial judge wrote: "I find that Matthews is an individual whose sense of identity and self-worth is highly connected to his work. He is a person who values honesty and integrity, and is willing to work hard in exchange for fair treatment and respect" (para. 292).

[11] Mr. Matthews' fortunes took a turn for the worse in 2007, when Ocean hired a new Chief Operating Officer, Daniel Emond. Frictions quickly developed between the two men. For whatever reason, the senior manager did not like Mr. Matthews, and did not consider him to be a valuable asset to Ocean. Mr. Emond was responsible for assigning responsibilities to Mr. Matthews, and he soon began what the trial judge characterized as a "campaign" to marginalize Mr. Matthews in the company (para. 296). This course of conduct went beyond decisions limiting Mr. Matthews' responsibilities, and included instances in which Mr. Emond "lied" to Mr. Matthews and Mr. Orr about his status and prospects with Ocean, "went behind [Mr. Matthews'] back", and "ignored Matthews' request to speak with him" relating to his role within the company (paras. 296-99). Indeed, the extensive findings of facts that the trial judge set out included repeated incidents of dishonesty attributed to senior management toward Mr. Matthews (paras. 291-326). While I will not repeat every detail, the following examples illustrate how Mr. Matthews was treated in the final years of his employment.

[12] The "first step in a campaign to push Matthews out of operations and minimize his influence" began in 2007, when Mr. Emond drastically reduced the number of people reporting to Mr. Matthews

Orr, a déclaré que [TRADUCTION] « [t]ous ceux qui ont tiré des bénéfices de l'existence d'Ocean le doivent pour la plupart dans une certaine mesure à [M. Matthews] » (voir 2017 NSSC 16, par. 66 (CanLII)).

[10] Monsieur Matthews était très investi dans son travail. En effet, le juge de première instance a écrit : [TRADUCTION] « Je suis d'avis que le sens de l'identité et l'estime de soi de M. Matthews sont étroitement liés à son travail. Il accorde une grande importance à l'honnêteté et à l'intégrité, et il est prêt à travailler fort pourvu qu'on le traite de façon équitable et avec respect » (par. 292).

[11] La situation de M. Matthews s'est détériorée en 2007 lorsque Ocean a embauché un nouveau directeur de l'exploitation, M. Daniel Emond. Il y a rapidement eu des frictions entre les deux hommes. Pour une raison quelconque, le directeur de l'exploitation n'aimait pas M. Matthews et ne le considérait pas comme un atout pour Ocean. Monsieur Emond, qui était chargé d'assigner à M. Matthews ses responsabilités, a rapidement entamé ce que le juge de première instance a qualifié de [TRADUCTION] « campagne » de marginalisation de M. Matthews au sein de l'entreprise (par. 296). Dans le cadre de cette campagne, M. Emond a non seulement pris des décisions limitant les responsabilités de M. Matthews, mais il a en outre [TRADUCTION] « menti » à quelques reprises à ce dernier et à M. Orr au sujet du statut et de l'avenir de M. Matthews au sein de l'entreprise, il « a agi dans [le] dos [de M. Matthews] » et il « a fait la sourde oreille à la demande de M. Matthews qui souhaitait discuter avec lui » de son rôle dans l'entreprise (par. 296-299). D'ailleurs, les abondantes conclusions de fait tirées par le juge de première instance font état d'actes répétés de malhonnêteté attribués à la haute direction envers M. Matthews (par. 291-326). Je n'entends pas relater de nouveau tous ces actes par le menu, mais les exemples suivants illustrent comment M. Matthews a été traité au cours des dernières années de son emploi.

[12] La [TRADUCTION] « première étape d'une campagne visant à écarter M. Matthews des opérations et à réduire au minimum son influence » a débuté en 2007 lorsque M. Emond a réduit de façon

(para. 296). Over the next four years, the trial judge observed that Mr. Matthews' responsibilities were reduced further, he became progressively more ostracized within the company, and Mr. Emond's conduct was characterized by dishonesty (e.g., see paras. 297-300). The trial judge explicitly found that Mr. Emond had "no qualms about leaving Matthews in a state of anxiety about his future", and that Mr. Matthews was left in a "prolonged state of anxiety and uncertainty" (paras. 317 and 341).

[13] At various times when confronted about decisions to transfer oversight away from Mr. Matthews or to change his reporting responsibilities, Mr. Emond would indeed lie to Mr. Matthews about his efforts to minimize the latter's role (see, e.g., paras. 296, 298 and 301). At one point, Mr. Emond wrote a letter to Mr. Matthews that purported to establish a reconciliation, acknowledging that their relationship had been "based on mistrust" and in which he undertook to be "more open and honest" with Mr. Matthews so he might be "respected by me" and by others in the company (see para. 114). The trial judge found that Mr. Emond's "use of the word 'honest' in the letter was intended to mean exactly that, with the implication being that he had been dishonest with Matthews in the past" (para. 301). These dishonest statements were relied upon by at least one other executive, who in turn developed "significant animosity" toward Mr. Matthews (paras. 286-87). Senior management also sought to exclude Mr. Matthews from various initiatives in which Mr. Matthews would normally participate, even if it was to the detriment of Ocean.

[14] In 2010, when Mr. Orr stepped away from running Ocean and became Chair of the Board of Directors, Mr. Matthews' situation worsened. Martin Jamieson assumed the role of President and Chief Executive Officer and, soon after his arrival, Mr. Matthews was placed under review. The trial

substantielle le nombre de personnes relevant de ce dernier (par. 296). Le juge de première instance a fait remarquer que, au cours des quatre années qui ont suivi, les responsabilités de M. Matthews ont été réduites encore plus, ce dernier devenant progressivement de plus en plus ostracisé au sein de l'entreprise, et M. Emond a adopté une conduite qui était entachée de malhonnêteté (voir, p. ex., par. 297-300). Le juge de première instance a explicitement conclu que M. Emond ne montrait [TRADUCTION] « aucun scrupule à laisser M. Matthews angoisser sur son avenir », et que M. Matthews a été plongé dans un « état prolongé d'angoisse et d'incertitude » (par. 317 et 341).

[13] À diverses occasions, lorsque M. Matthews l'a confronté au sujet des décisions qu'il prenait pour confier à d'autres certaines de ses tâches de supervision ou pour modifier ses responsabilités redditionnelles, M. Emond lui a effectivement menti à propos des efforts qu'il déployait pour réduire au minimum le rôle de celui-ci (voir, p. ex., par. 296, 298 et 301). À un certain moment, M. Emond a écrit à M. Matthews une lettre se voulant un effort de réconciliation, dans laquelle il reconnaissait que leur relation [TRADUCTION] « reposait sur la méfiance » et il s'engageait à être « plus ouvert et honnête » avec M. Matthews afin que ce dernier soit « respecté par [M. Emond] » et par d'autres dans l'entreprise (voir par. 114). Le juge de première instance a conclu qu'en [TRADUCTION] « utilisant le mot "honnête" M. Emond disait exactement ce qu'il voulait dire, ce qui impliquait qu'il avait été malhonnête avec M. Matthews par le passé » (par. 301). Au moins un autre cadre a cru à ces déclarations malhonnêtes et a par la suite développé une [TRADUCTION] « animosité considérable » envers M. Matthews (par. 286-287). La haute direction a également cherché à exclure celui-ci de divers projets auxquels il aurait généralement participé, et ce, même si son exclusion nuisait à Ocean.

[14] En 2010, lorsque M. Orr a quitté ses fonctions de président-directeur général d'Ocean et a assumé la présidence du conseil d'administration, la situation de M. Matthews s'est aggravée. Monsieur Martin Jamieson est alors devenu président-directeur général et, peu de temps après son entrée en fonction, la

judge found it had become clear that "Matthews' departure from [Ocean] was a possible consequence of the review" (para. 283). Around this time, Mr. Emond advised the Board of Directors there would soon be no place in the company for Mr. Matthews. When Mr. Orr informed him of these developments, Mr. Matthews' frustrations grew, as he was already suspicious that Ocean was conducting due diligence for a possible sale, a process in which he would normally have had a role but from which he found himself excluded.

[15] A potential sale of Ocean was significant, as it meant Mr. Matthews would be able to realize on Ocean's long term incentive plan ("LTIP"). The LTIP, a contractual arrangement providing for payment upon the sale of the company, proposed by Ocean and to which Mr. Matthews agreed in 2007, was designed for certain senior executives in service of two goals: to reward the participating employees for their previous contributions and provide an incentive to continue contributing to the company's success. Ocean's retention goal proved successful, as Mr. Matthews ended up staying longer than he would have otherwise. As the trial judge found, the LTIP was a "key reason" Mr. Matthews stayed with the company, particularly when his problems with senior management developed (para. 388).

[16] Mr. Matthews advised Mr. Emond that he wanted to stay in his role as he anticipated the company would soon be sold. Mr. Emond falsely told him he did not know what Ocean's plans were for him. He then sent an email to Mr. Jamieson, with the subject line "here we go again". It read in part:

Moreover [Matthews] also ask me if he is part of the restructuring???????? He said that he would like to stay as

place de M. Matthews dans l'entreprise a été examinée. Le juge de première instance a conclu qu'il était devenu évident que [TRADUCTION] « le départ de M. Matthews d'[Ocean] était une conséquence possible de cet examen » (par. 283). À cette époque, M. Emond a dit au conseil d'administration qu'il n'y aurait bientôt plus de place pour M. Matthews au sein de l'entreprise. Lorsque M. Orr a informé M. Matthews de ces propos, la frustration de ce dernier s'est accentuée, car il soupçonnait déjà Ocean d'avoir entamé un processus de diligence raisonnable en vue d'une possible vente, un processus dans lequel il aurait normalement dû jouer un rôle mais duquel il s'est retrouvé exclu.

[15] La possible vente d'Ocean était un événement important, car M. Matthews aurait alors pu obtenir la prime à laquelle il avait droit au titre du régime d'intéressement à long terme (« RILT ») d'Ocean. Le RILT — un arrangement contractuel prévoyant une forme de paiement en cas de vente de l'entreprise, qui avait été proposé par Ocean et signé par M. Matthews en 2007 — avait été conçu à l'intention de certains cadres supérieurs et visait deux objectifs : récompenser les employés parties au régime pour leurs contributions antérieures au succès de l'entreprise et les inciter à continuer de le faire. Ocean a réussi à atteindre son objectif de maintenir en poste son employé, puisque M. Matthews est demeuré au service de l'entreprise plus longtemps qu'il ne l'aurait fait autrement. Comme l'a conclu le juge de première instance, le RILT était une [TRADUCTION] « raison déterminante » dans la décision de M. Matthews de continuer de travailler pour l'entreprise, particulièrement lorsque ses problèmes avec la haute direction ont commencé (par. 388).

[16] Monsieur Matthews a informé M. Emond qu'il souhaitait conserver son rôle, car il s'attendait à ce que l'entreprise soit bientôt vendue. Monsieur Emond a faussement affirmé qu'il ne savait pas quelles étaient les intentions d'Ocean à son égard. Il a ensuite envoyé à M. Jamieson un courriel dont l'objet indiquait [TRADUCTION] « C'est reparti », et dans lequel il disait notamment ce qui suit :

De plus, [M. Matthews] m'a aussi demandé s'il fait partie de la restructuration???????? Il a dit qu'il aimerait rester

he believe the company will be sold to have is incentive on the sale?????? Anyway I manage to get myself out of it not sure he believe me but he got an answer. [Transcribed as in original.]

(See trial reasons, at para. 194.)

[17] A few months later, Mr. Matthews asked Mr. Jamieson whether Ocean was planning on terminating him. Mr. Jamieson told him the company had no such plans. Soon after, Mr. Matthews found himself meeting with the company's Vice President of Human Resources, discussing a possible termination package. Mr. Matthews advised the human resources representative that he would forfeit severance in order to protect his entitlement under the LTIP. In the end, however, negotiations over an "exit strategy" never came to fruition, as Mr. Matthews took a position with a new employer on June 22, 2011, officially leaving Ocean on June 24, 2011.

[18] About 13 months after Mr. Matthews' departure, Ocean was sold for $540 million. This constituted a "Realization Event" for the purposes of the LTIP, thus triggering payments to employees who qualified under the plan. But since Mr. Matthews was not actively employed on that date, Ocean took the position that he did not satisfy the terms of the plan. Accordingly, Mr. Matthews did not receive a payment. Notably, the trial judge found that Mr. Emond's mistreatment of Mr. Matthews was not motivated by a desire to deprive him of his LTIP entitlement, nor was there evidence of a company conspiracy to "get rid of Matthews in order to deprive him of his LTIP entitlement" (para. 325).

[19] Mr. Matthews filed an application against Ocean, alleging that his employer constructively dismissed him, behaved in a manner that was

parce qu'il croit que l'entreprise sera vendue et qu'il veut toucher sa prime en cas de vente?????? Quoi qu'il en soit j'ai réussi à m'en sortir je ne suis pas certain qu'il m'a cru mais il a eu une réponse. [Transcription de l'original.]

(Voir les motifs du jugement de première instance, par. 194.)

[17] Quelques mois plus tard, M. Matthews a demandé à M. Jamieson si Ocean prévoyait mettre fin à son emploi. Ce dernier lui a alors répondu que l'entreprise n'avait aucun plan de la sorte. Peu de temps après, M. Matthews a rencontré le vice-président des ressources humaines pour discuter d'un possible règlement forfaitaire de cessation d'emploi. Monsieur Matthews a dit au représentant des ressources humaines qu'il renoncerait à son indemnité de départ pour protéger ses droits au titre du RILT. Cependant, au bout du compte, les négociations sur une [TRADUCTION] « stratégie de départ » n'ont jamais abouti, étant donné que M. Matthews a accepté un poste chez un nouvel employeur le 22 juin 2011 et a quitté officiellement Ocean le 24 juin 2011.

[18] Environ 13 mois après le départ de M. Matthews, Ocean a été vendue pour la somme de 540 millions de dollars. Cette vente constituait, pour les besoins du RILT, [TRADUCTION] « [l']événement déclencheur », qui entraînait le versement des primes aux employés admissibles aux termes du régime. Toutefois, comme M. Matthews ne travaillait plus activement pour l'entreprise au moment de la vente, Ocean a soutenu qu'il ne satisfaisait pas aux conditions du régime. Monsieur Matthews n'a par conséquent pas reçu de prime. Fait notable, le juge de première instance a conclu que la conduite incorrecte de M. Emond envers M. Matthews n'était pas motivée par le désir de priver celui-ci du droit de recevoir le paiement prévu par le RILT, et qu'il n'y avait pas non plus de preuve que l'entreprise avait comploté pour [TRADUCTION] « se débarrasser de M. Matthews afin de le priver de ses droits au titre du RILT » (par. 325).

[19] Monsieur Matthews a présenté contre Ocean une requête dans laquelle il alléguait que son employeur l'avait congédié de façon déguisée et avait

"oppressive of, unfairly prejudicial to and in unfair disregard" of his interests, and, separately, that the constructive dismissal "was carried out in bad faith at law and in breach of the corporation's duty of good faith" (A.R., at p. 145). He sought the declaration alluded to earlier as well as loss of pay, bonuses and benefits, together with general damages, and compensation pursuant to an oppression remedy under s. 241(1) of the *Canada Business Corporation Act*, R.S.C. 1985, c. C-44. In light of Ocean's conduct that proceeded "in contum[e]lious disregard of [his] contractual entitlements" (A.R., at p. 145), Mr. Matthews also asked for punitive damages and solicitor and client costs.

agi d'une manière [TRADUCTION] « abusive, injustement préjudiciable et injustement indifférente » à l'égard de ses intérêts, puis il affirmait, dans une allégation distincte, que son congédiement déguisé « avait été effectué de mauvaise foi au sens de la loi et en contravention à l'obligation de la société d'agir de bonne foi » (d.a., p. 145). Il sollicitait la déclaration mentionnée plus tôt, des dommages-intérêts pour perte de revenus, de primes et d'avantages, des dommages-intérêts généraux ainsi qu'une indemnité à titre de réparation pour cause d'abus en vertu du par. 241(1) de la *Loi canadienne sur les sociétés par actions*, L.R.C. 1985, c. C-44. Compte tenu de la conduite d'Ocean, qui a manifesté [TRADUCTION] « une indifférence méprisante à l'égard [de ses] droits d'ordre contractuel » (d.a., p. 145), M. Matthews sollicitait également des dommages-intérêts punitifs et les dépens taxés sur la base procureur-client.

III. Prior Decisions

A. *Supreme Court of Nova Scotia (LeBlanc J.)*

[20] The trial judge concluded that Ocean constructively dismissed Mr. Matthews, and that Mr. Matthews was owed a reasonable notice period of 15 months. The trial judge relied upon this Court's decision in *Potter*, where Wagner J. explained that, typically, an employee's decision to leave their employment may be considered a constructive dismissal in two different ways. First, an employee may be prompted to leave because the employer substantially breached an express or implied term of the employment contract. Second, Wagner J. drew upon cases where "the employer's treatment of the employee made continued employment intolerable" (at para. 33), explaining that such cases will amount to constructive dismissal where the employer displayed, through its cumulative actions over time, that it no longer intended to be bound by the contract.

[21] The trial judge was satisfied that the test for constructive dismissal had been satisfied on either

III. Décisions des juridictions inférieures

A. *Cour suprême de la Nouvelle-Écosse (le juge LeBlanc)*

[20] Le juge de première instance a conclu qu'Ocean avait congédié M. Matthews de manière déguisée et que ce dernier avait droit à un préavis raisonnable de 15 mois. Le juge de première instance s'est appuyé sur l'arrêt *Potter* de notre Cour, dans lequel le juge Wagner a expliqué que, généralement, la décision d'un employé de quitter son emploi peut être considérée comme un congédiement déguisé dans deux situations différentes. Premièrement, un employé peut être poussé à quitter son emploi parce que son employeur a violé de manière substantielle une condition expresse ou tacite de son contrat de travail. Deuxièmement, s'appuyant sur d'autres affaires où « le comportement de l'employeur vis-à-vis du salarié avait rendu la situation intolérable au travail » (par. 33), le juge Wagner a expliqué que le départ de l'employé équivaudra à un congédiement déguisé lorsque l'employeur a manifesté, par l'effet cumulatif de ses actes antérieurs, son intention de ne plus être lié par le contrat.

[21] Le juge de première instance était convaincu qu'il y avait lieu de conclure au congédiement

branch articulated in *Potter*. With respect to the first branch, he concluded that it was an implied term that Mr. Matthews would be assigned work "which is substantially similar in terms of job duties, pay, responsibility and status" (para. 337, citing P. Barnacle, *Employment Law in Canada* (4th ed. (loose-leaf)), vol. 2, at §13.42). By unilaterally reducing Mr. Matthews' responsibilities in such a substantial manner, Ocean breached the employment contract.

[22] In terms of the second branch, the trial judge found that Ocean's senior manager "engaged in a course of conduct aimed at pushing Matthews out of operations and minimizing his influence and participation in the company", alluding to his findings of fact regarding Mr. Emond's deceit in respect of Mr. Matthews' future prospects with the company, as a result of which he "became increasingly ostracized" (para. 347). Given the behaviour, a reasonable person in Mr. Matthews' position would have felt that Ocean "had engaged in a course of conduct that evinced an intention [to] no longer . . . be bound by the contract" (para. 353).

[23] Relying on *Paquette v. TeraGo Networks Inc.*, 2016 ONCA 618, 352 O.A.C. 1, and *Lin v. Ontario Teachers' Pension Plan Board*, 2016 ONCA 619, 352 O.A.C. 10, the trial judge held that Mr. Matthews would have been a full-time employee when the Realization Event occurred had he not been constructively dismissed. Because the terms of the LTIP did not unambiguously limit or remove his common law right to damages, Mr. Matthews was entitled to damages equivalent to what he would have received under the LTIP.

[24] Given his conclusion on the LTIP, the trial judge wrote that it was unnecessary to decide whether Mr. Matthews was entitled to an equivalent amount pursuant to the oppression remedy (para. 418). The trial judge went on to reject Mr. Matthews' claim

déguisé suivant l'un ou l'autre des volets énoncés dans l'arrêt *Potter*. En ce qui concerne le premier volet, il a conclu qu'une condition tacite du contrat était que M. Matthews serait affecté à un poste [TRADUCTION] « dont les fonctions, la rémunération, les responsabilités et le statut seraient substantiellement similaires » (par. 337, citant P. Barnacle, *Employment Law in Canada* (4e éd. (feuilles mobiles)), vol. 2, §13.42). En réduisant unilatéralement les responsabilités de M. Matthews de manière aussi substantielle, Ocean a violé le contrat de travail.

[22] Pour ce qui est du deuxième volet, le juge de première instance a statué que le cadre supérieur d'Ocean [TRADUCTION] « a agi de façon à écarter M. Matthews des opérations et à réduire au minimum son influence et sa participation au sein de l'entreprise », se référant à ses conclusions de fait concernant la conduite trompeuse de M. Emond quant à l'avenir de M. Matthews dans l'entreprise, ce qui avait eu pour effet que ce dernier était « deven[u] de plus en plus ostracis[é] » (par. 347). Vu ce comportement, une personne raisonnable dans la situation de M. Matthews aurait estimé qu'Ocean [TRADUCTION] « agissait d'une manière démontrant [son] intention de ne plus être liée par le contrat » (par. 353).

[23] S'appuyant sur les arrêts *Paquette c. TeraGo Networks Inc.*, 2016 ONCA 618, 352 O.A.C. 1, et *Lin c. Ontario Teachers' Pension Plan Board*, 2016 ONCA 619, 352 O.A.C. 10, le juge de première instance a déclaré que M. Matthews aurait été un employé à temps plein de l'entreprise lorsque l'événement déclencheur s'est produit s'il n'avait pas été l'objet d'un congédiement déguisé. Comme les modalités du RILT n'avaient pas pour effet de limiter ou de supprimer clairement son droit à des dommages-intérêts en vertu de la common law, M. Matthews avait droit à des dommages-intérêts d'un montant équivalant au paiement qu'il aurait reçu en vertu du RILT.

[24] Compte tenu de sa conclusion au sujet du RILT, le juge de première instance a écrit qu'il était inutile de décider si M. Matthews avait droit à une somme équivalente à titre de réparation pour cause d'abus (par. 418). Le juge a également

for punitive damages, as he was not satisfied that Ocean's actions were directly motivated by a desire to deprive Mr. Matthews of his LTIP entitlement (para. 422).

[25] Based on his findings, the trial judge awarded Mr. Matthews lost earnings, $1,086,893.36 for the loss of the LTIP payment he would have received during the notice period, and other benefits, less an amount of $78,000 for mitigation of damages, representing monies paid to him by his new employer.

[26] The trial judge provided supplementary reasons regarding the quantum of damages during the reasonable notice period (2017 NSSC 123). A decision on costs was postponed pending a hearing on the matter. That was suspended while the case went to appeal.

B. *Court of Appeal of Nova Scotia (Farrar, Bryson and Scanlan JJ.A.)*

[27] The judges on appeal all agreed that Mr. Matthews' original claim for wrongful dismissal and for an oppression remedy had "morphed" into a case of constructive dismissal (2018 NSCA 44, 48 C.C.E.L. (4th) 171, at paras. 1 and 151). Accepting the trial judge's findings of fact, the Court of Appeal unanimously upheld his decision that Mr. Matthews had been constructively dismissed and that the appropriate reasonable notice period was 15 months. The judges differed, however, on the issue of damages and the relevance of good faith.

rejeté la demande de dommages-intérêts punitifs de M. Matthews, car il n'était pas convaincu que la conduite d'Ocean était directement motivée par le désir de priver M. Matthews de ses droits au titre du RILT (par. 422).

[25] Sur la base de ses conclusions, le juge de première instance a accordé à M. Matthews des dommages-intérêts pour sa perte de revenus, une somme de 1 086 893,36 $ pour la perte du paiement prévu par le RILT qu'il aurait reçu pendant la période de préavis et la perte d'autres avantages, moins une somme de 78 000 $ au titre de l'atténuation des dommages, qui correspondait à la rémunération que lui avait versée son nouvel employeur.

[26] Le juge de première instance a écrit des motifs supplémentaires relatifs au montant des dommages-intérêts qu'il convenait d'accorder pour la période de préavis raisonnable (2017 NSSC 123). La décision sur les dépens a été reportée jusqu'à la tenue d'une audience sur la question. Ce volet de l'affaire a été suspendu pendant la durée des procédures d'appel.

B. *Cour d'appel de la Nouvelle-Écosse (les juges Farrar, Bryson et Scanlan)*

[27] Les juges de la Cour d'appel étaient tous d'accord pour dire que l'action initiale de M. Matthews en congédiement injustifié et en réparation pour cause d'abus s'était [TRADUCTION] « transformée » en une action pour congédiement déguisé (2018 NSCA 44, 48 C.C.E.L. (4th) 171, par. 1 et 151). En acceptant les conclusions de fait du juge de première instance, la Cour d'appel a confirmé à l'unanimité la décision de celui-ci portant que M. Matthews avait fait l'objet d'un congédiement déguisé et que le préavis raisonnable approprié était de 15 mois. Les juges de la Cour d'appel ont toutefois différé d'opinions sur la question des dommages-intérêts et sur la pertinence de l'obligation d'agir de bonne foi.

(1) Majority Reasons (Farrar J.A., Bryson J.A. Concurring)

[28] The majority judges disagreed with the trial judge that Mr. Matthews was entitled to damages on account of the lost LTIP payment. The trial judge confused an employee's right to reasonable notice with an employee's ability to recover under an incentive plan. The proper question, they said, was "whether the employee qualifie[d] pursuant to the terms of the agreement" (para. 63).

[29] In their view, clause 2.03 of the LTIP was unambiguous, leading to the conclusion that Mr. Matthews' right to recover under the plan ceased the moment he left Ocean. They further held that clause 2.05 clearly stated that the LTIP could not be used for severance purposes, which, in their view, the trial judge had erroneously done. As was the case in *Styles v. Alberta Investment Management Corp.*, 2017 ABCA 1, 44 Alta. L.R. (6th) 214, the plain and unambiguous language of the LTIP therefore deprived Mr. Matthews of the opportunity to recover under the LTIP.

[30] The majority judges went on to comment on the dissenting reasons. First, they observed that "[t]his may have been a different case if the hearing judge had concluded that [Ocean] had orchestrated Matthews' termination to avoid any liability it might have under the [LTIP]", but this was rejected by the trial judge (paras. 89-90 and 114-16). In the majority's view, the dissenting judge ignored this key finding of fact. Second, the majority judges noted that it was open for the trial judge to award "additional damages as a result of the manner in which [Mr. Matthews] was treated", but "given his finding that there was no bad faith on the part of Ocean Nutrition, he could not and did not do so" (para. 122 (emphasis added)). Even though the majority judges found for Ocean in part and reversed one portion of

(1) Motifs de la majorité (le juge Farrar, avec l'accord du juge Bryson)

[28] Les juges majoritaires n'ont pas souscrit à l'opinion du juge de première instance suivant laquelle M. Matthews avait droit à des dommages-intérêts pour la perte du paiement prévu par le RILT. À leur avis, le premier juge avait confondu le droit d'un employé à un préavis raisonnable et la capacité d'un employé de toucher une prime en vertu d'un régime d'intéressement. La véritable question, selon les juges majoritaires, consistait plutôt à se demander [TRADUCTION] « si l'employé [était] admissible selon les modalités de l'entente » (par. 63).

[29] De l'avis des juges majoritaires, la clause 2.03 du RILT n'était pas ambiguë et permettait de conclure que M. Matthews a cessé d'avoir droit à la prime prévue par le régime dès qu'il a quitté Ocean. Ils ont en outre statué que la clause 2.05 indiquait clairement que le RILT ne pouvait pas être utilisé pour le calcul d'une indemnité de départ, ce qu'avait fait à tort le juge de première instance selon eux. Tout comme dans l'affaire *Styles c. Alberta Investment Management Corp.*, 2017 ABCA 1, 44 Alta. L.R. (6th) 214, le libellé clair et non ambigu du RILT privait donc M. Matthews de la possibilité de toucher une prime au titre de ce régime.

[30] Les juges majoritaires ont poursuivi en commentant les motifs de leur collègue dissident. Premièrement, ils ont fait remarquer que [TRADUCTION] « [l]'issue aurait été différente si le juge qui présidait l'audience avait conclu qu'[Ocean] avait orchestré la fin d'emploi de M. Matthews de manière à se soustraire à toute responsabilité qu'elle pourrait avoir aux termes du [RILT] », mais ce constat n'a pas été retenu par le juge de première instance (par. 89-90 et 114-116). De l'avis de la majorité, le juge dissident a fait abstraction de cette conclusion de fait cruciale. Deuxièmement, les juges majoritaires ont souligné qu'il était loisible au juge de première instance d'accorder [TRADUCTION] « des dommages-intérêts additionnels en raison de la manière dont [M. Matthews] avait été traité », mais

the judgment in first instance, it awarded no costs on appeal.

(2) Dissenting Reasons (Scanlan J.A.)

[31] Focusing principally on the allegations of mistreatment, the dissenting judge reasoned that the parties could not have "intended to agree that a rogue manager such as Emond could engineer the dismissal of a valued long-term employee through a series of lies, deceit and manipulation so as to result in that employee not being entitled to share in the value he was so essential in creating" (para. 148). Drawing on *Bhasin*, he held that "[t]here was an implied agreement that the LTIP and the employment contract would be performed with honesty and integrity" (para. 148). The dissenting judge explained his view that Mr. Emond's actions displayed the type of dishonesty contemplated in *Bhasin*:

> Neither party should be able to rely upon lies, deceit and manipulation to deny the other side of the benefits of the contractual relationship, even if that was not the primary goal of the party acting dishonestly. The hearing judge did not find that Ocean acted to intentionally deny Matthews' entitlement to the LTIP benefits, but my colleague says a consequence of Emond's action, which resulted in Matthews leaving, was the loss of the LTIP benefits. [para. 168]

The dissenting judge concluded that Ocean should therefore be held liable for any damages sustained as a result of that dishonesty.

[32] Justice Scanlan then presented a second path to recovery, again based on *Bhasin*. In his view, the

« comme il avait conclu à l'absence de mauvaise foi de la part d'Ocean Nutrition, il ne pouvait pas le faire et il ne l'a pas fait » (par. 122 (je souligne)). Même si les juges majoritaires ont partiellement statué en faveur d'Ocean et infirmé une partie du jugement rendu en première instance, ils n'ont pas adjugé de dépens en appel.

(2) Motifs dissidents (le juge d'appel Scanlan)

[31] S'attachant principalement aux allégations selon lesquelles M. Matthews avait été traité de façon incorrecte, le juge dissident a considéré que les parties ne pouvaient avoir eu [TRADUCTION] « l'intention de convenir qu'un directeur sans scrupules comme M. Emond puisse orchestrer le congédiement d'un employé estimé de longue date en usant de mensonges, de tromperies et de manipulations afin que cet employé n'ait pas le droit de toucher sa part d'une appréciation de valeur à laquelle il avait contribué de manière déterminante » (par. 148). Se fondant sur l'arrêt *Bhasin*, le juge dissident a déclaré [TRADUCTION] « [qu'il] existait un accord tacite portant que les modalités du RILT et du contrat de travail seraient exécutées avec honnêteté et intégrité » (par. 148). Il a expliqué ainsi son opinion selon laquelle les actes de M. Emond correspondaient au type d'actes malhonnêtes envisagés dans l'arrêt *Bhasin* :

> [TRADUCTION] Aucune partie ne devrait pouvoir user de mensonges, de tromperies et de manipulations pour refuser à l'autre les avantages découlant d'une relation contractuelle, et ce, même si ce n'était pas là l'objectif premier de la partie qui a agi malhonnêtement. Le juge qui présidait l'audience n'a pas conclu qu'Ocean avait agi intentionnellement afin de priver M. Matthews des avantages prévus par le RILT, mais mon collègue affirme qu'une des conséquences des actes de M. Emond, qui se sont traduits par le départ de M. Matthews, a été la perte de ces avantages. [par. 168]

Le juge dissident a conclu qu'Ocean devrait donc être tenue responsable de tout préjudice subi par M. Matthews en raison de cette malhonnêteté.

[32] Le juge Scanlan a ensuite exposé une autre voie permettant d'obtenir réparation, elle aussi

employment contract included an implied term of honest performance as part of the prohibition against unlawful dismissal without notice. Given that Ocean would benefit financially from Mr. Emond's deception, and by extension from Mr. Matthews' dismissal, the dissenting judge would have used the LTIP as a means to measure the damages for the constructive dismissal. This was appropriate since Ocean knew that a consequence of Mr. Matthews' dismissal was that his LTIP would be at risk, and that the sale of Ocean might soon occur. Consequently, the loss of opportunity to participate in the LTIP was a predictable loss. Based on these conclusions, he would "have awarded costs on this appeal to Matthews in the amount of 30% of appropriate trial costs" (para. 211).

fondée sur l'arrêt *Bhasin*. À son avis, le contrat de travail comprenait une condition tacite d'exécution honnête faisant partie de l'interdiction visant les congédiements illégaux sans préavis. Étant donné qu'Ocean tirerait un avantage pécuniaire de la tromperie de M. Emond, et, par extension, du congédiement de M. Matthews, le juge dissident aurait utilisé le RILT pour calculer le montant des dommages-intérêts pour le congédiement déguisé. Cette approche était appropriée, puisqu'Ocean savait que le congédiement de M. Matthews compromettrait les droits de ce dernier au titre du RILT, et qu'il était possible que la vente d'Ocean survienne sous peu. Par conséquent, la perte de l'occasion de toucher l'avantage prévu par le RILT était prévisible. Compte tenu de ces conclusions, le juge Scanlan aurait [TRADUCTION] « adjugé à M. Matthews des dépens en appel représentant 30 % du montant des dépens appropriés en première instance » (par. 211).

IV. Analysis

IV. Analyse

A. *Arguments on Appeal*

A. *Arguments en appel*

[33] On appeal, the parties continue to disagree as to the amount that should be paid to Mr. Matthews for damages, specifically whether he was entitled to compensation for the lost LTIP payment. This, in turn, reflects the disagreement between them as to the basis for awarding those damages — whether as a remedy for failure to provide reasonable notice or to act in good faith, or both. Respectfully stated, their arguments on appeal are confounding when placed side-by-side — not only do they address matters at cross-purposes but, at times, the parties seem to be speaking past one another.

[33] En appel, les parties ont continué d'exprimer leur désaccord quant au montant qui devrait être versé à M. Matthews au titre des dommages-intérêts, et, plus précisément, quant à la question de savoir si ce dernier avait droit d'être indemnisé pour la perte du paiement prévu par le RILT. Cette situation témoigne à son tour du désaccord qui existe entre les parties quant au fondement de l'octroi de dommages-intérêts — à savoir à titre de réparation pour l'absence de préavis raisonnable, pour le défaut d'agir de bonne foi, ou pour ces deux raisons. Avec égards, les arguments des parties en appel sont déroutants lorsque considérés côte à côte — non seulement ces arguments ne traitent-ils pas des mêmes questions, mais, par moment, les parties elles-mêmes semblent ne pas s'adresser l'une à l'autre.

[34] At the hearing, Mr. Matthews confined his arguments almost exclusively to the consequences of Ocean's alleged dishonesty. He argued that the majority of the Court of Appeal failed to recognize that Ocean, through its dishonest actions, breached the duty set forth in *Bhasin* "to ensure that the contract is performed in line with the organizing principle

[34] À l'audience, M. Matthews a limité ses arguments presque exclusivement aux conséquences de la malhonnêteté dont aurait fait preuve son employeur. Il a plaidé que les juges majoritaires de la Cour d'appel n'avaient pas tenu compte du fait que, par ses actes malhonnêtes, Ocean avait manqué à l'obligation formulée dans l'arrêt *Bhasin* [TRADUCTION] « de

of good faith and the duty of honest performance" (A.F., at para. 47). Relying on *Hadley v. Baxendale* (1854), 9 Ex. 341, 156 E.R. 145, Mr. Matthews submitted that, as a remedy for this breach, he was entitled to an amount equivalent to the LTIP payment. Moreover, he urged this Court to recognize good faith as animating the whole of the performance of the employment contract. This is relevant given what Mr. Matthews described as a "four-year course of lying to him about the status of his employment" (transcript, at p. 9).

[35] Mr. Matthews offered, secondarily, two further bases for his claim. First, he said, the majority of the Court of Appeal misdirected itself in failing to consider damages for Ocean's breach of its obligation to provide him with reasonable notice. Moreover, in light of the supposed breach of the duty of honest performance, Mr. Matthews argued, Ocean should have been barred from relying on the exclusionary clauses. In any event, Mr. Matthews said the LTIP was misread and the majority should have deferred to the trial judge's interpretation of that contract. Second, Mr. Matthews invoked the doctrine of estoppel to support his argument that Ocean cannot rely upon the exclusion clause.

[36] By contrast, Ocean focused on defending the exclusion of the LTIP as a matter of contractual interpretation. Ocean submitted that the bonus was not integral to Mr. Matthews' compensation. Further, it agreed with the majority of the Court of Appeal that the trial judge had misinterpreted the LTIP and that, given its plain and unambiguous language, the bonus should have been excluded from any damage award.

veiller à ce que le contrat soit exécuté en conformité avec le principe directeur de bonne foi et l'obligation d'agir honnêtement dans l'exécution des obligations contractuelles » (m.a., par. 47). S'appuyant sur l'arrêt *Hadley c. Baxendale* (1854), 9 Ex. 341, 156 E.R. 145, M. Matthews a affirmé qu'il avait droit à un montant correspondant au paiement prévu par le RILT à titre de réparation pour ce manquement. En outre, il a exhorté notre Cour à reconnaître que la bonne foi anime l'ensemble de l'exécution du contrat de travail. Cet argument est pertinent compte tenu de la situation que M. Matthews a décrite comme étant une [TRADUCTION] « campagne de quatre ans au cours de laquelle on lui a menti sur l'état de son emploi » (transcription, p. 9).

[35] À titre subsidiaire, M. Matthews a invoqué deux fondements additionnels au soutien de sa demande. Premièrement, il a affirmé que les juges majoritaires de la Cour d'appel se sont donné des directives erronées en omettant de considérer l'octroi de dommages-intérêts à l'égard du manquement d'Ocean de s'acquitter de son obligation de lui donner un préavis raisonnable. De plus, compte tenu du prétendu manquement à l'obligation d'exécution honnête, M. Matthews a fait valoir qu'Ocean n'aurait pas dû pouvoir invoquer les clauses d'exclusion. De toute façon, M. Matthews a déclaré que les juges majoritaires avaient mal interprété le RILT et qu'ils auraient dû s'en remettre à celle qu'en avait faite le juge de première instance. Deuxièmement, M. Matthews a invoqué la doctrine de la préclusion promissoire pour étayer son argument selon lequel Ocean ne pouvait pas appliquer la clause d'exclusion.

[36] En revanche, Ocean s'est attachée à défendre l'exclusion de M. Matthews du RILT comme étant une question d'interprétation contractuelle. Elle a fait valoir que la prime ne faisait pas partie intégrante de la rémunération de M. Matthews. De plus, à l'instar des juges majoritaires de la Cour d'appel, elle a exprimé l'avis que le juge de première instance a mal interprété le RILT et que, vu le libellé clair et non équivoque de ce document, la prime aurait dû être exclue de toute somme accordée au titre des dommages-intérêts.

[37] Ocean had little to say on good faith, except to acknowledge that the employer had displayed some "bad conduct" and to assert that there was no finding, at trial or in the majority opinion on appeal, of bad faith (transcript, at p. 66). After proposing a fresh characterization of certain facts relating to the interaction between Ocean's representatives and Mr. Matthews to that end, Ocean urged this Court to hold that the majority judges on appeal were right to conclude there was no bad faith. In any event, Ocean argued that the common law does not recognize any duties of good faith on the employer during the performance of the contract that could serve as a basis for the payment of the bonus.

[38] In these reasons, I seek to explain my view, respectfully stated, that the majority of the Court of Appeal erred in not awarding Mr. Matthews the amount of the LTIP as part of his common law damages for breach of the implied term to provide reasonable notice. In considering all of the complaints made by Mr. Matthews, it bears recalling that he did not seek damages for mental distress,[1] and while he originally pleaded for punitive damages, he did not pursue that head of damages on appeal in this Court. Consequently, it is unnecessary in the circumstances, and perhaps even unwise given the method on which *Bhasin* rests, to resolve Mr. Matthews' allegations of dishonest treatment since I propose to award him the only remedy sought on appeal — an amount equivalent to his LTIP entitlement — on the basis of reasonable notice. That said, Ocean's alleged dishonest behaviour over a protracted period, but in the manner

[37] Ocean a peu dit sur la question de la bonne foi, si ce n'est qu'elle a reconnu que l'employeur s'était à certains moments [TRADUCTION] « mal conduit » et qu'elle a affirmé que ni le juge de première instance ni les juges majoritaires de la Cour d'appel n'avaient conclu à la mauvaise foi (transcription, p. 66). Après avoir proposé, au soutien de cette affirmation, une nouvelle qualification de certains faits liés aux interactions entre les représentants d'Ocean et M. Matthews, Ocean a demandé à notre Cour de statuer que les juges majoritaires de la Cour d'appel avaient eu raison de conclure à l'absence de mauvaise foi. Quoi qu'il en soit, Ocean a soutenu que la common law n'impose à l'employeur aucune obligation d'agir de bonne foi dans l'exécution du contrat qui pourrait servir de fondement justifiant le paiement de la prime en question.

[38] Je m'efforce, dans les présents motifs, d'expliquer, avec égards pour l'opinion contraire, mon point de vue selon lequel les juges majoritaires de la Cour d'appel ont fait erreur en n'incluant pas le montant de la prime prévue par le RILT dans les dommages-intérêts qui ont été accordés à M. Matthews, en vertu de la common law, pour le manquement à l'obligation tacite de lui donner un préavis raisonnable. Dans l'examen de l'ensemble des griefs invoqués par M. Matthews, il convient de rappeler que ce dernier n'a pas sollicité de dommages-intérêts pour souffrances morales[1], et que bien qu'il ait demandé des dommages-intérêts punitifs initialement, il n'a pas continué de réclamer ce chef de dommages-intérêts devant notre Cour. Par conséquent, il n'est pas nécessaire dans les circonstances, et il serait peut-être même peu judicieux vu la méthode suivie dans l'arrêt *Bhasin*, de statuer sur les allégations de malhonnêteté

[1] The term "aggravated damages" was used on occasion by the two parties throughout this appeal. I note, however, that in *Fidler v. Sun Life Assurance Co. of Canada*, 2006 SCC 30, [2006] 2 S.C.R. 3, at paras. 52-54, this Court explained that this term is largely a misnomer, and that compensatory damages for a contractual breach of the duty of good faith spoken to in *Wallace* "are based on what was in the reasonable contemplation of the parties at the time of contract formation".

[1] L'expression [TRADUCTION] « dommages-intérêts majorés » a été employée à l'occasion par les deux parties tout au long du présent pourvoi. Je fais remarquer toutefois que, dans l'arrêt *Fidler c. Sun Life du Canada, compagnie d'assurance-vie*, 2006 CSC 30, [2006] 2 R.C.S. 3, par. 52-54, notre Cour a expliqué que cette expression est en grande partie inexacte, et que les dommages-intérêts compensatoires accordés pour le manquement à l'obligation contractuelle d'agir de bonne foi dont il a été question dans l'arrêt *Wallace* « sont fondés sur ce que les parties pouvaient raisonnablement envisager au moment de la formation du contrat ».

of dismissal nonetheless, attracts a brief comment. I come to this view for two reasons.

[39] The first pertains to the proper method of analyzing claims for wrongful dismissal, like that of Mr. Matthews, where the employee alleges a failure to provide reasonable notice as well as bad faith. So long as damages are appropriately made out and causation established, a breach of a duty of good faith could certainly give rise to distinct damages based on the principles in *Hadley*, approved in this setting in *Keays* (at paras. 55-56), including damages for mental distress. Punitive damages could also be available in certain circumstances. To this end, ensuring litigants take care that their pleadings are properly made out, and ensuring courts are following a methodologically coherent approach to constructive dismissal cases is certainly of value as it can affect the ultimate damage amount to be awarded to an employee plaintiff.

[40] It is apparent too from the pleadings here that there is a measure of uncertainty as to the impact of *Bhasin*, not just in Mr. Matthews' case but on employment law more generally. At a minimum, I believe this is an occasion to re-affirm two important principles stated in *Potter*. First, given the various submissions in this case, I would recall that the duty of honest performance — which Cromwell J. explained in *Bhasin* applies to all contracts, and means simply that parties "must not lie [to] or otherwise knowingly mislead" their counterparty "about matters directly linked to the performance of the

avancées par M. Matthews, étant donné que je propose de lui accorder la seule réparation sollicitée en appel — soit une somme équivalente au paiement auquel il a droit en vertu du RILT — sur la base du droit à un préavis raisonnable. Cela dit, quelques observations s'imposent à l'égard des allégations relatives à la conduite malhonnête qu'aurait eue Ocean pendant une période prolongée, mais néanmoins liée aux circonstances du congédiement. J'arrive à cette conclusion pour deux raisons.

[39] La première se rapporte à la méthode qu'il convient d'utiliser pour analyser les actions pour congédiement injustifié, comme celle de M. Matthews, lorsque l'employé prétend qu'on ne lui a pas donné un préavis raisonnable et qu'il y a eu mauvaise foi. Tant que la preuve du préjudice est apportée comme il se doit et que l'existence d'un lien de causalité est établie, un manquement à l'obligation d'agir de bonne foi pourrait certainement donner ouverture à des dommages-intérêts distincts selon les principes établis dans l'arrêt *Hadley*, qui ont été approuvés dans ce contexte dans l'arrêt *Keays* (par. 55-56), notamment des dommages-intérêts pour souffrances morales. Des dommages-intérêts punitifs pourraient également être accordés dans certaines circonstances. À cette fin, il est certes important que les parties s'assurent que leurs actes de procédure sont formulés adéquatement et que les tribunaux appliquent une approche cohérente sur le plan méthodologique lorsqu'ils instruisent des poursuites pour congédiement déguisé, car tout cela peut influer sur le montant des dommages-intérêts qui est accordé en définitive à l'employé demandeur.

[40] De plus, il ressort de l'argumentation des parties en l'espèce qu'une part d'incertitude plane en ce qui a trait à l'incidence de l'arrêt *Bhasin*, non seulement sur le pourvoi de M. Matthews, mais aussi sur le droit de l'emploi en général. Je crois que la présente affaire constitue à tout le moins une occasion de réaffirmer deux principes importants énoncés dans l'arrêt *Potter*. Premièrement, vu les divers arguments avancés par les parties, je tiens à rappeler que l'obligation d'exécution honnête — qui, comme l'a expliqué le juge Cromwell dans l'arrêt *Bhasin*, s'applique à tous les contrats et signifie simplement que

contract" — is applicable to employment contracts (*Bhasin*, at para. 33, see also para. 73; *Potter*, at para. 99). Second, given the four-year period of alleged dishonesty leading up to Mr. Matthews' dismissal, I would also reiterate that when an employee alleges a breach of the duty to exercise good faith in the manner of dismissal — a phrase introduced by this Court in *Wallace*, and reinforced in *Keays* — this means courts are able to examine a period of conduct that is not confined to the exact moment of termination itself. All this reflects, in my view, settled law.

les parties « ne doivent pas se mentir » les unes aux autres « ni s'induire intentionnellement en erreur au sujet des questions directement liées à l'exécution du contrat » — est applicable aux contrats de travail (*Bhasin*, par. 33, voir aussi par. 73; *Potter*, par. 99). Deuxièmement, je prends bonne note de la période de quatre ans au cours de laquelle il y aurait eu comportement malhonnête à l'endroit de M. Matthews avant son congédiement. En conséquence, je tiens également à réitérer que, dans les cas où un employé prétend qu'il y a eu manquement à l'obligation d'agir de bonne foi dans la façon de procéder au congédiement — formule introduite par notre Cour dans l'arrêt *Wallace*, puis réaffirmée dans l'arrêt *Keays* —, il s'ensuit que les tribunaux sont autorisés à examiner une conduite qui s'est échelonnée sur une certaine période et qui ne se limite pas au moment précis où il a été mis fin à l'emploi. À mon avis, tous ces aspects constituent des règles de droit bien établies.

[41] The second reason relates to the qualitatively different types of the contractual breaches alleged from the start by Mr. Matthews. This difference was addressed, in some measure, in *Keays* when it was determined that the breach in question should not, as was sometimes the case, simply bump-up the reasonable notice period.[2] To say that one has been treated dishonestly is quite unlike saying that one has been dismissed without notice. This is directly relevant to Mr. Matthews' call for the courts to declare that he was mistreated by Ocean.

[41] La deuxième raison se rapporte aux types qualitativement différents de manquements contractuels qui ont été invoqués par M. Matthews dès le départ. Dans une certaine mesure, cette différence a été considérée dans l'arrêt *Keays* où il a été jugé que le manquement en question ne devrait pas, comme c'était parfois le cas, servir simplement à allonger la durée de la période de préavis raisonnable[2]. Dire qu'un employé a été traité malhonnêtement est très différent de dire qu'il a été congédié sans préavis. Cette constatation est directement pertinente dans le cas de la demande adressée par M. Matthews aux tribunaux afin d'obtenir une déclaration portant qu'il a été traité de façon incorrecte par Ocean.

B. *The Appropriate Method of Analysis*

B. *Méthode d'analyse appropriée*

[42] Properly understood, the claim pursued here indeed rests on allegations of distinct contractual breaches of Mr. Matthews' employment contract.

[42] Interprétée adéquatement, l'action débattue en l'espèce repose en effet sur des allégations reprochant deux manquements distincts au contrat de travail de M. Matthews.

[2] K. Banks, "Progress and Paradox: The Remarkable yet Limited Advance of Employer Good Faith Duties in Canadian Common Law" (2011), 32 *Comp. Lab. L. & Pol'y J.* 547, at pp. 561-62.

[2] K. Banks, « Progress and Paradox : The Remarkable yet Limited Advance of Employer Good Faith Duties in Canadian Common Law » (2011), 32 *Comp. Lab. L. & Pol'y J.* 547, p. 561-562.

[43] Neither party disputes that, at common law, an employer has the right to terminate the employment contract without cause — or, in this case, prompt the employee to choose to leave their job in circumstances that amount to a dismissal — subject to the duty to provide reasonable notice, a right which, as this Court noted in *Farber v. Royal Trust Co.*, [1997] 1 S.C.R. 846, at para. 23, is reciprocal in the contract of employment. When breached, the obligation to provide reasonable notice does not, in theory, turn on the presence or absence of good faith: it is, in a manner of speaking, a "good faith" wrongful dismissal (see *Machtinger*, at p. 990). The contractual breach that arises from the employer's choice in this regard is simply the failure to provide reasonable notice, which leads to an award of damages in lieu thereof (*Wallace*, at para. 115, per McLachlin J., as she then was, dissenting, but not on this point). There is some dispute in the cases regarding how to determine what damages should be awarded in the event of a breach, which I will consider below, but this breach does not turn on whether or not the employer acted honestly or in good faith.

[44] Running parallel to the argument on reasonable notice, Mr. Matthews has alleged that his termination was also in breach of contract because it failed to meet the expected standard of good faith. Under rules recognized by this Court in *Bhasin* and *Potter*, an unhappy employee can allege dishonesty in the performance of the contract by the employer — i.e., a breach of the duty of honest performance, which Cromwell J. in *Bhasin* described as contractual doctrine — independently of any failure to provide reasonable notice. This Court has also recognized in *Wallace* and *Keays* that an unhappy employee can allege mistreatment — i.e., conduct that is "unfair or is in bad faith by being, for example, untruthful, misleading or unduly insensitive" — in the manner

[43] Ni l'une ni l'autre des parties ne contestent le fait, que suivant la common law, un employeur a le droit de résilier un contrat de travail sans motif — ou, comme c'est le cas en l'espèce, de pousser un employé à quitter son emploi dans des circonstances qui équivalent à un congédiement — pourvu que cet employeur s'acquitte de son obligation de donner un préavis raisonnable, droit qui, comme l'a souligné la Cour dans l'arrêt *Farber c. Cie Trust Royal*, [1997] 1 R.C.S. 846, par. 23, est réciproque en matière de contrat de travail. En cas de manquement à l'obligation de donner un préavis raisonnable, la question qui se pose n'est pas, en théorie, de savoir s'il y a eu ou non bonne foi; il s'agit, pour ainsi dire, d'un congédiement injustifié effectué de « bonne foi » (voir *Machtinger*, p. 990). Le manquement au contrat découlant de la décision de l'employeur à cet égard est simplement le défaut de donner un préavis raisonnable, situation qui entraîne le paiement de dommages-intérêts tenant lieu de préavis (*Wallace*, par. 115, la juge McLachlin (plus tard juge en chef), dissidente, mais non sur ce point). Il existe, dans la jurisprudence, un certain désaccord sur la façon de calculer le montant des dommages-intérêts qui devraient être accordés en cas de manquement, désaccord que j'aborderai plus loin; cependant, ce manquement ne dépend pas de la réponse à la question de savoir si l'employeur a agi avec honnêteté ou de bonne foi.

[44] Parallèlement à son argument fondé sur la question du préavis raisonnable, M. Matthews prétend que la façon dont on a mis fin à son emploi contrevenait également au contrat de travail en ce qu'on n'a pas respecté la norme de bonne foi attendue. En vertu des règles qui ont été reconnues par notre Cour dans les arrêts *Bhasin* et *Potter*, un employé mécontent peut alléguer que son employeur a agi de façon malhonnête dans l'exécution du contrat — c.-à-d., qu'il y a eu manquement à l'obligation d'exécution honnête, ce que le juge Cromwell dans *Bhasin* a qualifié de doctrine du droit des contrats — indépendamment de tout manquement à l'obligation de donner un préavis raisonnable. Notre Cour a également reconnu, dans les arrêts

of dismissal by the employer (*Wallace*, at para. 98; *Keays*, at para. 57). A breach of the duty to exercise good faith in the manner of dismissal is also independent of any failure to provide reasonable notice. It can serve as a basis to answer for foreseeable injury that results from callous or insensitive conduct in the manner of dismissal, a point to which I will return to at the conclusion of these reasons (*Wallace*, at para. 88).

[45] Importantly, damages arising out of the same dismissal are calculated differently depending on the breach invoked. Again, this is nothing but a reflection of settled law. In *Keays*, at para. 56, for example, Bastarache J. helpfully explained that "[t]he contract of employment is, by its very terms, subject to cancellation on notice or subject to payment of damages in lieu of notice without regard to the ordinary psychological impact of that decision". By contrast, he explained that failure to act in good faith during the manner of dismissal "can lead to foreseeable, compensable damages" based on the *Hadley* principle (para. 58). Contrary to what had been thought until that time, an extension of the notice period was not to be used to determine the proper amount to be paid (para. 59). This is because the nature of the contractual breach is of a different order than that associated with the failure to provide reasonable notice. Indeed, it is this fundamental difference that explains why principles of mitigation apply differently to mental distress damages flowing from a breach of the good faith obligation in the manner of dismissal (*Evans v. Teamsters Local Union No. 31*, 2008 SCC 20, [2008] 1 S.C.R. 661, at para. 32).

Wallace et *Keays*, qu'un employé mécontent peut alléguer qu'il a été traité de façon incorrecte dans la façon dont on l'a congédié — c.-à-d., que l'employeur s'est comporté « de façon inéquitable ou [a fait] preuve de mauvaise foi en étant, par exemple, menteur [. . .], trompeur [. . .] ou trop implacable » (*Wallace*, par. 98; *Keays*, par. 57). Un manquement à l'obligation d'agir de bonne foi dans la façon de congédier l'employé est également indépendant de tout manquement à l'obligation de donner un préavis raisonnable. Il peut servir de moyen permettant d'exiger réparation à l'égard d'un préjudice prévisible résultant d'un traitement brutal ou implacable de la part de l'employeur dans la façon dont il a congédié l'employé, point sur lequel je reviendrai à la fin des présents motifs (*Wallace*, par. 88).

[45] Fait important, les dommages-intérêts découlant d'un même congédiement sont calculés différemment selon la violation reprochée. Je le répète, ce fait n'est que le reflet de la jurisprudence déjà établie. Dans l'arrêt *Keays*, par. 56, par exemple, le juge Bastarache a utilement expliqué que, « [s]uivant son libellé, le contrat d'emploi est susceptible de résiliation moyennant préavis ou paiement d'une indemnité en tenant lieu, indépendamment du préjudice psychologique normal causé par une telle mesure ». Par comparaison, il a précisé que si l'employeur n'agit pas de bonne foi lorsqu'il congédie un employé, « il y aura préjudice prévisible susceptible d'indemnisation » suivant le principe établi dans l'arrêt *Hadley* (par. 58). Contrairement à ce que l'on croyait avant cette affaire, il n'y a pas lieu d'allonger le préavis pour déterminer le juste montant de l'indemnité (par. 59). Il en est ainsi parce que la nature du manquement au contrat n'est pas du même ordre que dans le cas du défaut de donner un préavis raisonnable. En effet, cette distinction fondamentale permet d'expliquer pourquoi les principes relatifs à l'atténuation des dommages s'appliquent différemment aux dommages-intérêts pour souffrances morales imputables à un manquement à l'obligation d'agir de bonne foi dans la façon de procéder au congédiement (*Evans c. Teamsters Local Union No. 31*, 2008 CSC 20, [2008] 1 R.C.S. 661, par. 32).

[46] With this in mind, I turn now to examine the duty to provide reasonable notice, which as will become plain, is dispositive of this appeal.

(1) Duty to Provide Reasonable Notice

[47] In the case at bar, the only disagreement in respect of reasonable notice turns on whether Mr. Matthews' damages include an amount to compensate him for his lost LTIP payment.

[48] In my respectful view, the majority of the Court of Appeal erred by focusing on whether the terms of the LTIP were "plain and unambiguous" instead of asking what damages were appropriately due for Ocean's failure to provide Mr. Matthews with reasonable notice. The issue is not whether Mr. Matthews is entitled to the LTIP in itself, but rather what damages he is entitled to and whether he was entitled to compensation for bonuses he would have earned had Ocean not breached the employment contract. By focusing narrowly on the former question, the Court of Appeal applied an incorrect principle, resulting in what I see as an overriding error.

(a) *Redress for Breach of the Implied Term to Provide Reasonable Notice of Termination*

[49] Insofar as Mr. Matthews was constructively dismissed without notice, he was entitled to damages representing the salary, including bonuses, he would have earned during the 15-month period (*Wallace*, at paras. 65-67). This is so because the remedy for a breach of the implied term to provide reasonable notice is an award of damages based on the period of notice which should have been given, with the damages representing "what the employee would have earned in this period" (para. 115). Whether payments under incentive bonuses, such as the LTIP in this case, are to be included in these damages is a

[46] Gardant ces considérations à l'esprit, j'examinerai maintenant l'obligation de donner un préavis raisonnable, obligation qui, comme il ressortira clairement, permet de trancher le présent pourvoi.

(1) Obligation de donner un préavis raisonnable

[47] En l'espèce, le seul désaccord quant au préavis raisonnable porte sur la question de savoir si les dommages-intérêts accordés à M. Matthews doivent inclure une somme l'indemnisant pour la perte du paiement prévu par le RILT.

[48] Je suis respectueusement d'avis que les juges majoritaires de la Cour d'appel ont commis une erreur en s'attachant à la question de savoir si les modalités du RILT étaient [TRADUCTION] « claires et non ambiguës » au lieu de s'interroger sur le montant des dommages-intérêts qu'il convenait d'accorder à M. Matthews parce qu'Ocean ne lui a pas donné un préavis raisonnable. Il ne s'agit pas de décider si M. Matthews est admissible au RILT, mais plutôt de déterminer le montant des dommages-intérêts auquel il a droit et s'il a droit d'être indemnisé pour les primes qu'il aurait touchées si Ocean n'avait pas contrevenu au contrat de travail. En se concentrant sur la première question, la Cour d'appel a appliqué un mauvais principe, ce qui a à mon avis entraîné une erreur déterminante.

a) *Réparation pour manquement à l'obligation tacite de donner un préavis raisonnable de cessation d'emploi*

[49] Dans la mesure où M. Matthews a fait l'objet d'un congédiement déguisé sans préavis, il avait droit à des dommages-intérêts correspondant au salaire, y compris les primes, qu'il aurait touché durant la période de préavis de 15 mois (*Wallace*, par. 65-67). Il en est ainsi parce que la réparation en cas de manquement à l'obligation tacite de donner un préavis raisonnable consiste à accorder des dommages-intérêts fondés sur la période du préavis qui aurait dû être donné, dommages-intérêts correspondant « au montant que l'employé aurait gagné pendant cette période » (par. 115). La question de

common and recurring issue in the law of wrongful dismissal. To answer this question, the trial judge relied on *Paquette* and *Lin* from the Court of Appeal for Ontario. I believe he took the right approach.

[50] In *Paquette*, the employee participated in his employer's bonus plan, which stipulated that employees had to be "actively employed" on the date of the bonus payout. That language is broadly comparable to that found in the LTIP which, at clause 2.03, requires the claimant to be a "full-time employee" of the company. In *Paquette*, but for the employee's termination, the employee would have received the bonus within the reasonable notice period. The motion judge in that case, however, concluded that the employee was not entitled to the bonus because, while he may have been "notionally" employed during the reasonable notice period, he was not "actively" employed and so did not qualify under the terms of the plan.

[51] The employee's appeal was allowed. The Ontario Court of Appeal relied principally on its prior decision in *Taggart v. Canada Life Assurance Co.* (2006), 50 C.C.P.B. 163, concerning a similar question related to pension benefits. In that case, Sharpe J.A. rightly cautioned that courts should not ignore the legal nature of employees' claims. "The claim is not", he said, "for the pension benefits themselves. Rather, it is for common law contract damages as compensation for the pension benefits [the employee] would have earned had [the employer] not breached the contract of employment" (para. 16). Consequently, "a terminated employee is entitled to claim damages for the loss of pension benefits that would have accrued had the employee worked until the end of the notice period" (para. 13). With respect to the role of a bonus plan's contractual terms, Sharpe J.A. explained that "[t]he question at this

savoir si les sommes à verser au titre d'un régime d'intéressement, tel le RILT en l'espèce, doivent être incluses dans les dommages-intérêts est une question courante et récurrente dans le domaine du droit applicable au congédiement injustifié. Pour répondre à cette question, le juge de première instance s'est appuyé sur les arrêts *Paquette* et *Lin* de la Cour d'appel de l'Ontario. J'estime qu'il a choisi la bonne approche.

[50] Dans l'arrêt *Paquette*, l'employé participait au régime de primes établi par son employeur, lequel stipulait que les employés devaient être des [TRADUCTION] « employés actifs » à la date du versement des primes. Cette formulation est sensiblement comparable à celle utilisée dans le RILT qui, à la clause 2.03, requiert que l'intéressé soit un [TRADUCTION] « employé à temps plein » de l'entreprise. Dans l'arrêt *Paquette*, n'eût été son congédiement, l'employé aurait touché la prime à laquelle il avait droit pendant la période de préavis raisonnable. Cependant, dans cette affaire, le juge des motions a conclu que l'employé n'avait pas droit à la prime en question, parce que même s'il était [TRADUCTION] « théoriquement » un employé de l'entreprise pendant la période de préavis raisonnable, il n'était pas un employé « actif » et n'était donc pas admissible suivant les modalités du régime.

[51] L'appel de l'employé a été accueilli. La Cour d'appel de l'Ontario s'est appuyée principalement sur sa décision antérieure dans l'affaire *Taggart c. Canada Life Assurance Co.* (2006), 50 C.C.P.B. 163, qui portait sur une question similaire concernant les prestations de retraite. Dans cet arrêt, le juge d'appel Sharpe a, à juste titre, mis en garde les tribunaux de ne pas faire abstraction de la nature juridique des réclamations des employés. Comme il l'a indiqué, [TRADUCTION] « [l]a réclamation ne porte pas sur les prestations de retraite elles-mêmes. Elle vise plutôt l'obtention de dommages-intérêts contractuels en common law à titre de dédommagement pour les prestations de retraite auxquels [l'employé] aurait eu droit si [l'employeur] n'avait pas contrevenu au contrat de travail » (par. 16). Par conséquent, [TRADUCTION] « un employé congédié a le droit de réclamer des dommages-intérêts pour la perte de

stage is whether there is something in the language of the pension contract between the parties that takes away or limits that common law right" (para. 20).

[52] The Court of Appeal in *Paquette* built upon the approach in *Taggart*, proposing that courts should take a two-step approach to these questions. First, courts should "consider the [employee's] common law rights" (para. 30). That is, courts should examine whether, but for the termination, the employee would have been entitled to the bonus during the reasonable notice period. Second, courts should "determine whether there is something in the bonus plan that would specifically remove the [employee's] common law entitlement" (para. 31). "The question", van Rensburg J.A. explained, "is not whether the contract or plan is ambiguous, but whether the wording of the plan unambiguously alters or removes the [employee's] common law rights" (para. 31).

[53] I agree with van Rensburg J.A. that this is the appropriate approach. It accords with basic principles of damages for constructive dismissal, anchoring the analysis around reasonable notice. As the court recognized in *Taggart*, and reiterated in *Paquette*, when employees sue for damages for constructive dismissal, they are claiming for damages as compensation for the income, benefits, and bonuses they would have received had the employer not breached the implied term to provide reasonable notice (see also *Iacobucci v. WIC Radio Ltd.*, 1999 BCCA 753, 72 B.C.L.R. (3d) 234, at paras. 19 and 24; *Gillies v. Goldman Sachs Canada Inc.*, 2001 BCCA 683, 95 B.C.L.R. (3d) 260, at paras. 10-12 and 25; *Keays*, at paras. 54-55). Proceeding directly

prestations de retraite auxquelles il aurait eu droit s'il avait travaillé jusqu'à la fin de la période de préavis » (par. 13). En ce qui concerne le rôle des modalités contractuelles d'un régime de primes, le juge d'appel Sharpe a expliqué que [TRADUCTION] « [l]a question à cette étape consiste à décider s'il y a quelque chose dans le texte des modalités du régime de retraite existant entre les parties qui a pour effet de supprimer ou de limiter ce droit que confère la common law » (par. 20).

[52] Dans l'arrêt *Paquette*, la Cour d'appel s'est inspirée de l'approche adoptée dans l'arrêt *Taggart* et a proposé que les tribunaux appliquent une démarche en deux étapes à l'égard de ces questions. Premièrement, les tribunaux devraient [TRADUCTION] « considérer les droits dont dispose [l'employé] en vertu de la common law » (par. 30). En d'autres mots, les tribunaux devraient se demander si, n'eût été son congédiement, l'employé aurait eu le droit de toucher la prime en litige pendant la période de préavis raisonnable. Deuxièmement, les tribunaux devraient [TRADUCTION] « déterminer s'il y a quelque chose dans les modalités du régime de primes qui prive expressément [l'employé] des droits que lui confère la common law » (par. 31). Comme l'a expliqué la juge d'appel van Rensburg, [TRADUCTION] « [l]a question n'est pas de savoir si le contrat ou le régime est ambigu, mais plutôt de savoir s'il y a quelque chose dans le texte des modalités du régime qui modifie ou supprime clairement les droits reconnus à [l'employé] par la common law » (par. 31).

[53] Tout comme la juge van Rensburg, je suis d'avis qu'il s'agit de la démarche appropriée. Elle est conforme aux principes fondamentaux applicables aux dommages-intérêts pour congédiement déguisé, l'analyse s'attachant à la question du préavis raisonnable. Comme la cour l'a reconnu dans l'arrêt *Taggart*, et réitéré dans l'arrêt *Paquette*, lorsque des employés intentent une action en dommages-intérêts pour congédiement déguisé, ils sollicitent des dommages-intérêts à titre de dédommagement pour le revenu, les prestations et les primes qu'ils auraient touchés si l'employeur n'avait pas manqué à son obligation tacite de donner un préavis raisonnable (voir aussi *Iacobucci c. WIC Radio Ltd.*, 1999 BCCA 753, 72 B.C.L.R. (3d) 234, par. 19

to an examination of contractual terms divorces the question of damages from the underlying breach, which is an error in principle.

[54] Moreover, the approach in *Paquette* respects the well-established understanding that the contract effectively "remains alive" for the purposes of assessing the employee's damages, in order to determine what compensation the employee would have been entitled to but for the dismissal (see, e.g., *Nygard Int. Ltd. v. Robinson* (1990), 46 B.C.L.R. (2d) 103 (C.A.), at pp. 106-7, per Southin J.A., concurring; *Gillies*, at para. 17).

[55] Courts should accordingly ask two questions when determining whether the appropriate quantum of damages for breach of the implied term to provide reasonable notice includes bonus payments and certain other benefits. Would the employee have been entitled to the bonus or benefit as part of their compensation during the reasonable notice period? If so, do the terms of the employment contract or bonus plan unambiguously take away or limit that common law right?

(b) *Application to Mr. Matthews' Case*

[56] The first question is whether Mr. Matthews would have been entitled to the LTIP payment as part of his compensation during the reasonable notice period. Since the Realization Event was triggered within the 15-month reasonable notice period, Mr. Matthews argues that he is *prima facie* entitled to damages for the lost LTIP payment as part of his common law damages.

[57] Ocean argues that Mr. Matthews cannot satisfy the first stage of the analysis. It points this Court

et 24; *Gillies c. Goldman Sachs Canada Inc.*, 2001 BCCA 683, 95 B.C.L.R. (3d) 260, par. 10-12 et 25; *Keays*, par. 54-55). Procéder directement à l'examen des modalités contractuelles a pour effet de dissocier la question des dommages-intérêts du manquement sous-jacent, ce qui constitue une erreur de principe.

[54] En outre, la démarche suivie dans l'arrêt *Paquette* est compatible avec l'interprétation bien établie selon laquelle le contrat [TRADUCTION] « demeure [effectivement] en vigueur » pour les besoins de l'évaluation du préjudice de l'employé en vue de calculer le montant de l'indemnité à laquelle ce dernier aurait eu droit n'eût été son congédiement (voir, p. ex., *Nygard Int. Ltd. c. Robinson* (1990), 46 B.C.L.R. (2d) 103 (C.A.), p. 106-107, motifs concordants de la juge d'appel Southin; *Gillies*, par. 17).

[55] Les tribunaux devraient en conséquence se poser deux questions lorsqu'ils sont appelés à décider si le montant des dommages-intérêts qu'il convient d'accorder pour manquement à l'obligation tacite de donner un préavis raisonnable doit inclure les primes et certains autres avantages. L'employé aurait-il eu droit à la prime ou à l'avantage dans le cadre de ses conditions de rémunération pendant la période de préavis raisonnable? Dans l'affirmative, les modalités du contrat de travail ou du régime de primes ont-elles pour effet de supprimer ou de limiter clairement ce droit que confère la common law?

b) *Application au cas de M. Matthews*

[56] La première question consiste à se demander si M. Matthews aurait eu droit au paiement prévu par le RILT dans le cadre de ses conditions de rémunération pendant la période de préavis raisonnable. Comme l'événement déclencheur s'est produit pendant la période de préavis raisonnable de 15 mois, M. Matthews soutient qu'il a droit, à première vue, au titre des dommages-intérêts fondés sur la common law, à des dommages-intérêts pour la perte du paiement prévu par le RILT.

[57] Ocean affirme que M. Matthews n'est pas en mesure de satisfaire à la première étape de l'analyse.

to *Singer v. Nordstrong Equipment Limited*, 2018 ONCA 364, 47 C.C.E.L. (4th) 218, where the Court of Appeal for Ontario presented the first question by asking whether the bonus was "an integral part of his compensation package" (para. 21). Relying on this formulation, Ocean contends that, under the first step, Mr. Matthews has a common law entitlement to damages for all compensation and benefits that are integral to his compensation. Ocean maintains that the LTIP payment was not integral to Mr. Matthews' compensation since he did not have a vested right at the date of termination.

Elle invoque l'arrêt *Singer c. Nordstrong Equipment Limited*, 2018 ONCA 364, 47 C.C.E.L. (4th) 218, dans lequel la Cour d'appel de l'Ontario, à l'étape de la première question, s'est demandée si la prime [TRADUCTION] « faisait partie intégrante des conditions de rémunération [de l'intéressé] » (par. 21). S'appuyant sur cette formulation, Ocean prétend que, selon la première étape, la common law confère à M. Matthews le droit de recevoir des dommages-intérêts pour le salaire et les avantages qui font partie intégrante de sa rémunération. Elle soutient que le paiement prévu par le RILT ne faisait pas partie intégrante de la rémunération de M. Matthews, car ce dernier n'avait pas un droit acquis sur ce paiement lorsque son emploi a pris fin.

[58] The trial judge confronted this submission and concluded that Ocean was attempting to introduce an extra requirement into the analysis that is not supported by the jurisprudence (para. 387). I agree. The test of whether a benefit or bonus is "integral" to the employee's compensation assists in answering the question of what the employee would have been paid during the reasonable notice period (see, e.g., *Brock v. Matthews Group Ltd.* (1988), 20 C.C.E.L. 110 (Ont. H.C.J.), at p. 123, aff'd (1991), 34 C.C.E.L. 50 (C.A.); *Paquette*, at para. 17). Thus, in *Paquette* and *Singer*, where the bonuses at issue were discretionary, the Court of Appeal for Ontario considered this so-called "integral" test since there was doubt as to whether the employee would have received those discretionary bonuses during the reasonable notice period.

[58] Le juge de première instance s'est arrêté à cet argument et a conclu qu'Ocean cherchait à introduire dans l'analyse une exigence supplémentaire qui n'est pas étayée par la jurisprudence (par. 387). Je suis d'accord. Le critère qui consiste à déterminer si un avantage ou une prime fait « partie intégrante » de la rémunération d'un employé aide à répondre à la question de savoir ce qui aurait été payé à cet employé pendant la période de préavis raisonnable (voir, p. ex., *Brock c. Matthews Group Ltd.* (1988), 20 C.C.E.L. 110 (H.C.J. Ont.), p. 123, conf. par (1991), 34 C.C.E.L. 50 (C.A.); *Paquette*, par. 17). Ainsi, dans les arrêts *Paquette* et *Singer*, où les primes en litige étaient discrétionnaires, la Cour d'appel de l'Ontario a pris en compte ce critère, dit de la « partie intégrante », car un doute subsistait quant à la question de savoir si l'employé aurait touché ces primes discrétionnaires pendant la période de préavis raisonnable.

[59] This case is different. The purpose of damages in lieu of reasonable notice is to put the employee in the position they would have been in had they continued to work through to the end of the notice period. It is uncontested that the Realization Event occurred during the notice period. But for Mr. Matthews' dismissal, he would have received an LTIP payment during that period. In such circumstances, there is no need to ask whether the LTIP payment was "integral" to his compensation.

[59] La présente affaire est différente. Les dommages-intérêts tenant lieu de préavis raisonnable ont pour objet de rétablir l'employé dans la situation où il se serait trouvé s'il avait continué de travailler jusqu'à la fin de la période de préavis. Il n'est pas contesté que l'événement déclencheur s'est produit pendant cette période. Cependant, n'eût été son congédiement, M. Matthews aurait reçu le paiement prévu par le RILT durant cette période. Dans ces circonstances, il est inutile de se demander si ce paiement faisait « partie intégrante » de sa rémunération.

[60] Furthermore, in answer to a question from one of my colleagues at the hearing, counsel for Ocean conceded that Mr. Matthews may well have had an entitlement to the LTIP absent clauses 2.03 and 2.05. I am thus satisfied that, on this first step, Mr. Matthews is *prima facie* entitled to receive damages as compensation for the lost bonus.

[61] On the second step, the question is whether the terms of the LTIP unambiguously limit or remove Mr. Matthews' common law right. It should be mentioned that the parties took opposing positions on the applicable standard of review for questions related to the interpretation of the LTIP. Both parties relied on *Ledcor Construction Ltd. v. Northbridge Indemnity Insurance Co.*, 2016 SCC 37, [2016] 2 S.C.R. 23. For his part, Mr. Matthews argued that the trial judge's interpretation should be reviewed for palpable and overriding error. Ocean, in contrast, said that the standard of review should be correctness, relying on the standard form contract exception described in *Ledcor*. Ocean stressed that there is no evidence that Mr. Matthews negotiated the relevant terms, and that the LTIP applies to multiple employees.

[62] I am careful to note that the trial judge did not find that this was a commonly-used standard form agreement. In *Ledcor*, the Court was tasked with interpreting a standard form agreement commonly used in the insurance industry, where "consistency [in interpretation] is particularly important" (para. 40). Justice Wagner explained that, given that standard form contracts are those that are so widely used that the "interpretation of the . . . contract could affect many people" (at para. 39), a standard form exception is appropriate. This case is different: the only relevant finding by the trial judge on this issue is that it was "a limited number of executives" that were affected by the LTIP (para. 61). In the end, however, it is not necessary to decide whether or not the LTIP was truly a standard form contract in this case,

[60] Qui plus est, en réponse à une question de l'un de mes collègues lors de l'audience, l'avocate d'Ocean a reconnu que M. Matthews aurait fort bien pu avoir droit au paiement prévu par le RILT en l'absence des clauses 2.03 et 2.05. Je suis donc convaincu que, au terme de la première étape, M. Matthews a droit, à première vue, de recevoir des dommages-intérêts à titre de dédommagement pour la prime qu'il a perdue.

[61] À la deuxième étape, la question consiste à se demander si les modalités du RILT ont pour effet de limiter ou de supprimer clairement le droit que confère la common law à M. Matthews. Il convient de mentionner que les parties ont avancé des thèses opposées en ce qui a trait à la norme de contrôle applicable aux questions liées à l'interprétation du RILT. Les deux parties ont invoqué l'arrêt *Ledcor Construction Ltd. c. Société d'assurance d'indemnisation Northbridge*, 2016 CSC 37, [2016] 2 R.C.S. 23. Pour sa part, M. Matthews a plaidé que l'interprétation du juge de première instance devait être contrôlée afin de déterminer si elle renferme des erreurs manifestes et déterminantes. À l'opposé, s'appuyant sur l'exception relative au contrat type qui est décrite dans l'arrêt *Ledcor*, Ocean a soutenu que la norme de contrôle applicable était celle de la décision correcte. Elle a insisté sur le fait qu'il n'y a aucune preuve indiquant que M. Matthews aurait négocié les modalités pertinentes du RILT, et que ce régime s'applique à de nombreux employés.

[62] Je prends bonne note du fait que le juge de première instance n'a pas conclu que le RILT était un contrat type couramment utilisé. Dans l'arrêt *Ledcor*, la Cour était appelée à interpréter un contrat type qui est couramment utilisé dans le secteur des assurances, où « la constance [dans l'interprétation] revêt une importance particulière » (par. 40). Le juge Wagner a expliqué que, comme les contrats types sont largement utilisés et que « l'interprétation du contrat [. . .] peut toucher de nombreuses personnes » (par. 39), il convient d'appliquer une exception à l'égard des contrats types. La présente affaire est différente : la seule conclusion pertinente qu'a tirée le juge de première instance sur ce point est [TRADUCTION] « [qu']un nombre limité de cadres supérieurs » étaient visés par le RILT (par. 61). En

since the trial judge did not consider one of the two main clauses at issue in this case, clause 2.05, which therefore must be interpreted in any event.

[63] Returning, then, to the main clauses at issue, which provide the following:

2.03 CONDITIONS PRECEDENT:

ONC shall have no obligation under this Agreement to the Employee unless on the date of a Realization Event the Employee is a full-time employee of ONC. For greater certainty, this Agreement shall be of no force and effect if the employee ceases to be an employee of ONC, regardless of whether the Employee resigns or is terminated, with or without cause.

2.05 GENERAL:

The Long Term Value Creation Bonus Plan does not have any current or future value other than on the date of a Realization Event and shall not be calculated as part of the Employee's compensation for any purpose, including in connection with the Employee's resignation or in any severance calculation.

[64] The question is not whether these terms are ambiguous but whether the wording of the plan unambiguously limits or removes the employee's common law rights (*Paquette*, at para. 31, citing *Taggart*, at paras. 12 and 19-22). Importantly, given that the LTIP is a "unilateral contract", in the sense that the parties did not negotiate its terms, the principle of contractual interpretation that clauses excluding or limiting liability will be strictly construed "applies with particular force" (*Taggart*, at para. 18, citing *Hunter Engineering Co. v. Syncrude Canada Ltd.*, [1989] 1 S.C.R. 426, at p. 459). As this Court recognized in *Tercon Contractors Ltd. v. British Columbia (Transportation and Highways)*, 2010 SCC 4, [2010] 1 S.C.R. 69, at para. 73, albeit in the commercial context, and cited here to underscore just this point,

définitive, cependant, il n'est pas nécessaire en l'espèce de décider si le RILT était véritablement un contrat type, étant donné que le juge de première instance a omis de tenir compte de l'une des deux principales clauses litigieuses dans la présente affaire, soit la clause 2.05, qu'il faudra en conséquence interpréter de toute façon.

[63] Je reviens donc aux principales clauses litigieuses, qui sont rédigées ainsi :

[TRADUCTION]

2.03 CONDITIONS PRÉALABLES

ONC n'a, aux termes de la présente entente, aucune obligation envers l'employé à moins que ce dernier ne soit un employé à temps plein d'ONC lorsque survient l'événement déclencheur. Il est entendu que la présente entente est nulle et sans effet si l'employé cesse d'être un employé d'ONC, que ce soit parce qu'il démissionne ou parce qu'il est congédié, avec ou sans motif.

2.05 GÉNÉRALITÉS

Le Régime de primes pour la création de valeur à long terme n'a aucune valeur actuelle ou future si ce n'est à la date de l'événement déclencheur et la prime calculée et versée à l'employé ne doit pas être considérée comme faisant partie de la rémunération de ce dernier à quelque fin que ce soit, y compris en cas de démission de l'employé ou de calcul de toute indemnité de départ.

[64] Il ne s'agit pas de déterminer si ces modalités sont ambiguës, mais de savoir si le texte du régime a pour effet de limiter ou de supprimer clairement les droits que confère la common law à l'employé (*Paquette*, par. 31, citant *Taggart*, par. 12 et 19-22). Fait important, comme le RILT est un [TRADUCTION] « contrat unilatéral », en ce sens que les parties n'ont pas négocié ses modalités, le principe d'interprétation des contrats selon lequel les clauses d'exonération ou de limitation de responsabilité doivent recevoir une interprétation stricte [TRADUCTION] « s'applique avec une vigueur singulière » (*Taggart*, par. 18, citant *Hunter Engineering Co. c. Syncrude Canada Ltée*, [1989] 1 R.C.S. 426, p. 459). Comme l'a reconnu notre Cour dans *Tercon Contractors Ltd. c. Colombie-Britannique (Transports et Voirie)*,

sophisticated parties are able to draft clear and comprehensive exclusion clauses when they are minded to do so.

[65] To this end, the provisions of the agreement must be absolutely clear and unambiguous. So, language requiring an employee to be "full-time" or "active", such as clause 2.03, will not suffice to remove an employee's common law right to damages. After all, had Mr. Matthews been given proper notice, he would have been "full-time" or "actively employed" throughout the reasonable notice period (*Paquette*, at para. 33, citing *Schumacher v. Toronto-Dominion Bank* (1997), 147 D.L.R. (4th) 128 (Ont. C.J. (Gen. Div.)), at p. 184; see also para. 47; *Lin*, at para. 89). Indeed, the trial judge and the majority of the Court of Appeal agreed that an "active employment" requirement is not sufficient to limit an employee's damages (trial reasons, at para. 398; C.A. reasons, at para. 66).

[66] Similarly, where a clause purports to remove an employee's common law right to damages upon termination "with or without cause", such as clause 2.03, this language will not suffice. Here, Mr. Matthews suffered an *unlawful* termination since he was constructively dismissed without notice. As this Court held in *Bauer v. Bank of Montreal*, [1980] 2 S.C.R. 102, at p. 108, exclusion clauses "must clearly cover the exact circumstances which have arisen". So, in Mr. Matthews' case, the trial judge properly recognized that "[t]ermination without cause does not imply termination without notice" (para. 399; see also *Veer v. Dover Corp. (Canada) Ltd.* (1999), 120 O.A.C. 394, at para. 14; *Lin*, at para. 91). Yet, it bears repeating that, for the purpose of calculating wrongful dismissal damages, the employment contract is not treated as "terminated" until after the reasonable notice period expires. So,

2010 CSC 4, [2010] 1 R.C.S. 69, par. 73, décision rendue en contexte commercial, et qui est mentionnée en l'espèce uniquement pour souligner le point suivant : des parties expérimentées peuvent rédiger des clauses à la fois claires et exhaustives d'exonération lorsqu'elles entendent le faire.

[65] Pour cette raison, les dispositions de l'entente doivent être absolument claires et non ambiguës. Ainsi, une disposition exigeant qu'un employé soit un [TRADUCTION] « employé à temps plein » ou un « employé actif » de l'entreprise, comme l'exige la clause 2.03, ne sera pas suffisante pour supprimer le droit que confère la common law à un employé d'obtenir des dommages-intérêts. Après tout, si un préavis adéquat avait été donné à M. Matthews, ce dernier aurait été un « employé à temps plein » ou un « employé actif » de l'entreprise pendant la période de préavis raisonnable (*Paquette*, par. 33, citant *Schumacher c. Toronto-Dominion Bank* (1997), 147 D.L.R. (4th) 128 (C.J. Ont. (Div. gén.)), p. 184; voir également par. 47; *Lin*, par. 89). D'ailleurs, le juge de première instance et les juges majoritaires de la Cour d'appel ont reconnu qu'une condition stipulant que l'employé soit en situation [TRADUCTION] « [d']emploi actif » n'est pas suffisante pour limiter les dommages-intérêts auxquels un employé a droit (motifs de première instance, par. 398; motifs de la Cour d'appel, par. 66).

[66] De même, lorsqu'une clause vise à supprimer le droit qu'a un employé en vertu de la common law d'obtenir des dommages-intérêts lorsqu'il est congédié « avec ou sans motif », comme le prévoit la clause 2.03, une telle disposition ne sera pas suffisante. En l'espèce, M. Matthews a fait l'objet d'un congédiement *illégal* étant donné qu'il a été congédié de manière déguisée sans préavis. Comme l'a conclu notre Cour dans l'arrêt *Bauer c. Banque de Montréal*, [1980] 2 R.C.S. 102, p. 108, « il doit être évident que [les clauses d'exclusion] vise[nt] les circonstances exactes qui se présentent ». Par conséquent, dans le cas de M. Matthews, le juge de première instance a reconnu à juste titre [TRADUCTION] « [qu'un] congédiement sans motif n'implique pas un congédiement sans préavis » (par. 399; voir également *Veer c. Dover Corp. (Canada) Ltd.* (1999), 120 O.A.C. 394, par. 14; *Lin*, par. 91). Or, il

even if the clause had expressly referred to an unlawful termination, in my view, this too would not unambiguously alter the employee's common law entitlement.

[67] I therefore agree with the trial judge that clause 2.03 does not unambiguously limit or remove Mr. Matthews' common law right. In my respectful view, the majority of the Court of Appeal erred in concluding otherwise.

[68] As mentioned, it is true that the trial judge did not expressly consider clause 2.05. The dissenting judge suggested this clause only prevents Mr. Matthews from seeking the bonus as part of his severance, and not part of a claim for wrongful dismissal damages. The majority disagreed, arguing there is no functional difference between severance and damages (paras. 120-21).

[69] I respectfully disagree with the majority of the Court of Appeal on this point. The trial judge did not use the LTIP to calculate severance; rather, he determined the quantum of damages that Mr. Matthews was entitled to under the common law following the constructive dismissal. As the dissenting judge explained in detail, severance and damages are distinct legal concepts. The primary purpose of providing reasonable notice (or damages in lieu thereof) is to protect employees by providing them an opportunity to seek alternative employment (see *Wallace*, at para. 120, per McLachlin J. (as she then was) dissenting, but not on this point). Severance pay, by contrast, "acts to compensate long-serving employees for their years of service and investment in the employer's business and for the special losses they suffer when their employment terminates", and is often provided

convient de répéter que, pour les besoins du calcul du montant des dommages-intérêts à verser en cas de congédiement injustifié, le contrat de travail est considéré comme étant « résilié » uniquement après l'expiration de la période de préavis raisonnable. Par conséquent, même si la clause en question avait fait mention expressément d'un congédiement illégal, je suis d'avis qu'une telle disposition n'aurait pas non plus modifié clairement le droit que confère la common law à l'employé.

[67] Ainsi, à l'instar du juge de première instance, j'estime que la clause 2.03 n'a pas pour effet de limiter ou de supprimer clairement le droit que confère la common law à M. Matthews. Je suis respectueusement d'avis que les juges majoritaires de la Cour d'appel ont commis une erreur en tirant une conclusion différente.

[68] Comme je l'ai mentionné, il est vrai que le juge de première instance n'a pas explicitement examiné la clause 2.05. Le juge dissident a précisé que cette clause empêche seulement M. Matthews de demander que la prime fasse partie de son indemnité de départ, et non des dommages-intérêts pour congédiement injustifié qu'il réclame. Les juges majoritaires ont exprimé leur désaccord à cet égard, affirmant qu'il n'existe aucune différence, du point de vue de la fonction, entre une indemnité de départ et des dommages-intérêts (par. 120-121).

[69] Avec égards, je ne puis me rallier à l'opinion des juges majoritaires de la Cour d'appel sur ce point. Le juge de première instance n'a pas utilisé le RILT pour calculer l'indemnité de départ; il a plutôt déterminé le montant des dommages-intérêts auxquels M. Matthews avait droit en vertu de la common law par suite de son congédiement déguisé. Comme l'a expliqué en détail le juge dissident, l'indemnité de départ et les dommages-intérêts sont des concepts juridiques distincts. Le principal objectif d'un préavis raisonnable (ou de dommages-intérêts en tenant lieu) est de protéger l'employé en lui fournissant l'occasion de se chercher un autre emploi (voir *Wallace*, par. 120, la juge McLachlin (plus tard juge en chef), dissidente, mais non sur ce point). En revanche, l'indemnité de cessation d'emploi « vient indemniser les employés ayant beaucoup d'années

for in provincial employment standards legislation (*Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 S.C.R. 27, at para. 26).

[70] Moreover, clause 2.05 must be read as a whole; it also states that the LTIP "does not have any current or future value other than on the date of a Realization Event". If Mr. Matthews had been properly given notice of termination, he would have remained a full-time employee on the date of the Realization Event, and thus would have received an LTIP payment. His damages reflect that lost opportunity.

[71] In reaching a different conclusion regarding the interpretation of clauses 2.03 and 2.05, the majority judges relied on *Styles* from the Court of Appeal of Alberta. Ocean urges this Court to do the same. While this is not the occasion to examine the law in Alberta in depth, I allow myself the following observations.

[72] At issue in *Styles* was a similar question to the one here: was the employee, upon being terminated without cause, entitled to receive a payment under his employer's contractual long-term incentive plan? Upon termination, the employer paid the employee a lump sum payment equal to three months' salary pursuant to the terms of his employment contract (*Styles v. Alberta Investment Corp.*, 2015 ABQB 621, [2016] 4 W.W.R. 593, at paras. 9 and 27, per Yungwirth J.). The bonus would not have vested until several *years* after the employee's termination (paras. 17-23). Consequently, the employee could not recover damages for a payment under the bonus in connection to the reasonable notice period. At a minimum, *Styles* is thus distinguishable from Mr. Matthews' case. The latter raises issues surrounding damages connected to the notice period, while the former does not.

de service pour ces années investies dans l'entreprise de l'employeur et pour les pertes spéciales qu'ils subissent lorsqu'ils sont licenciés », et elle est souvent prévue dans les lois provinciales sur les normes d'emploi (*Rizzo & Rizzo Shoes Ltd. (Re)*, [1998] 1 R.C.S. 27, par. 26).

[70] En outre, la clause 2.05 doit être considérée globalement; elle précise également que le RILT « n'a aucune valeur actuelle ou future si ce n'est à la date de l'événement déclencheur ». Si M. Matthews avait reçu un préavis de congédiement adéquat, il aurait toujours été un employé à temps plein de l'entreprise à la date de l'événement déclencheur et il aurait alors reçu le paiement prévu par le RILT. Les dommages-intérêts qui lui ont été accordés tiennent compte de cette occasion manquée.

[71] Pour arriver à une conclusion différente quant à l'interprétation des clauses 2.03 et 2.05, les juges majoritaires se sont appuyés sur l'arrêt *Styles* de la Cour d'appel de l'Alberta. Ocean exhorte notre Cour à faire de même. Bien que le présent pourvoi ne soit pas l'occasion d'examiner en profondeur les règles de droit applicables en Alberta, je me permets de faire les observations qui suivent.

[72] Dans l'arrêt *Styles*, la question en litige était similaire à celle qui se pose en l'espèce : après avoir été congédié sans motif, l'employé avait-il le droit de recevoir un paiement en vertu du régime d'intéressement à long terme de son employeur? Après le congédiement, l'employeur a versé à l'employé un paiement forfaitaire correspondant à trois mois de salaire conformément aux modalités de son contrat de travail (*Styles c. Alberta Investment Corp.*, 2015 ABQB 621, [2016] 4 W.W.R. 593, par. 9 et 27, la juge Yungwirth). La prime n'aurait été acquise au profit de l'employé que plusieurs *années* après son congédiement (par. 17-23). Par conséquent, l'employé ne pouvait pas obtenir des dommages-intérêts pour la prime qui lui aurait été versée pendant la période de préavis raisonnable. À tout le moins, l'affaire *Styles* se distingue donc de cette façon du cas de M. Matthews. En effet, la situation de ce dernier soulève des questions concernant les dommages-intérêts liés à la période de préavis, alors que ce n'est pas le cas dans l'arrêt *Styles*.

[73] It also bears noting that the Court of Appeal of Alberta in *Styles* suggested that *Paquette*, one of the cases I rely on here, is premised upon an erroneous reading of this Court's decision in *Sylvester v. British Columbia*, [1997] 2 S.C.R. 315. In *Styles*, the Court of Appeal noted that "[t]he common law implies a term of reasonable notice, or pay in lieu, in those circumstances. The payment in lieu is not 'damages' for a breach of the contract, but rather one component of the compensation provided for in the contract. If an employer fails to give proper notice or pay in lieu, the breach is in the failure to pay, not in the termination" (para. 34 (footnote omitted)). The Court of Appeal then observed that "[t]here are decisions from other jurisdictions that treat termination as a breach, but they do not reflect the law of Alberta: see for example [*Paquette*]. *Paquette* relies on the *dictum* in [*Sylvester*], at para. 1, but para. 15 of that decision confirms that it is the non-payment that is the breach, not the termination itself" (para. 34, fn. 1).

[74] On my reading, this Court in *Sylvester* confirmed that "[d]amages for wrongful dismissal are designed to compensate the employee for the breach by the employer of the implied term in the employment contract to provide reasonable notice of termination" (para. 15 (emphasis added)). Authority elsewhere confirms this same idea: there is no such implied term of the contract to provide payment in lieu (see, e.g., *Love v. Acuity Investment Management Inc.*, 2011 ONCA 130, 277 O.A.C. 15, at para. 44).[3]

[73] Il convient également de souligner que la Cour d'appel de l'Alberta, dans l'affaire *Styles*, a indiqué que l'arrêt *Paquette*, l'un des arrêts sur lesquels je m'appuie en l'espèce, repose sur une interprétation erronée de la décision de notre Cour dans *Sylvester c. Colombie-Britannique*, [1997] 2 R.C.S. 315. Dans l'arrêt *Styles*, la Cour d'appel a fait remarquer [TRADUCTION] « [qu'il] existe en common law une condition tacite selon laquelle un préavis raisonnable, ou une indemnité en tenant lieu, doit être fourni dans ces circonstances. L'indemnité tenant lieu de préavis raisonnable ne constitue pas des "dommages-intérêts" pour violation du contrat, mais plutôt une portion de l'indemnité prévue au contrat. Si un employeur ne donne pas un préavis adéquat ou une indemnité en tenant lieu, la violation réside dans le non-paiement d'une indemnité et non dans le congédiement » (par. 34 (note en bas de page omise)). La Cour d'appel a ensuite souligné que, [TRADUCTION] « [d]ans certaines décisions rendues dans d'autres ressorts, le congédiement est considéré comme une violation, mais ces décisions ne reflètent pas le droit albertain : voir, par exemple [*Paquette*]. Dans cet arrêt, le tribunal s'appuie sur la remarque incidente formulée dans [*Sylvester*], au par. 1, mais le par. 15 de cette décision confirme que c'est le non-paiement qui constitue la violation, et non le congédiement lui-même » (par. 34, note 1).

[74] Selon mon interprétation, notre Cour a confirmé dans l'arrêt *Sylvester* que « [l]es dommages-intérêts versés pour congédiement injustifié visent à indemniser l'employé à l'égard de la violation par l'employeur de la condition implicite du contrat d'emploi selon laquelle ce dernier doit donner à l'employé un préavis raisonnable de cessation d'emploi » (par. 15 (je souligne)). Cette même idée est d'ailleurs confirmée par d'autres sources dans d'autres ressorts : le contrat ne comporte aucune condition implicite selon laquelle l'employeur doit verser une indemnité tenant lieu de préavis (voir, p. ex., *Love c. Acuity Investment Management Inc.*, 2011 ONCA 130, 277 O.A.C. 15, par. 44)[3].

[3] See D. D. Buchanan, "Defining Wrongful Dismissal: The Alberta Schism" (2019), 57 *Alta. L. Rev.* 95.

[3] Voir D. D. Buchanan, « Defining Wrongful Dismissal : The Alberta Schism » (2019), 57 *Alta. L. Rev.* 95.

[75] As explained by the Court of Appeal for British Columbia in *Dunlop v. B.C. Hydro & Power Authority* (1988), 32 B.C.L.R. (2d) 334, at pp. 338-39, there are three principal reasons why this is an important distinction. First, there are issues surrounding the complexity of an implied term to provide pay in lieu of notice, and whether such a term can readily be implied into an employment contract. Second, implying a term to provide pay in lieu of notice "would mean that if an employer elected to give pay in lieu of notice, the employer would be complying with the contract and not breaking it", and thus "the contract would require the full payment to be made immediately". Third, if the employer elected to invoke such an implied term and gave no notice of termination, "there would be no obligation on the part of the employee to mitigate damages by seeking other employment" since the term requires a payment in full without regard to the employee's actual losses. Ensuring that courts and litigants properly understand this distinction is thus important as it can profoundly affect employees' financial lives. To the extent that some cases suggest otherwise, I respectfully disagree.

[76] Finally, at this stage of the analysis, it may also be appropriate in certain cases to examine whether the clauses purporting to limit or take away an employee's common law right were adequately brought to the employee's attention (*Paquette*, at para. 18; *Taggart*, at paras. 20-23; *Poole v. Whirlpool Corp.*, 2011 ONCA 808, 97 C.C.E.L. (3d) 20, at paras. 5-6). This issue, however, does not arise on these facts. Moreover, as several interveners commented on in this appeal, it may be appropriate to question whether the clause at issue is compatible with minimum employment standards (*Machtinger*, at p. 1004). This issue was not canvassed by the courts below and, in the present circumstances, it is unnecessary to explore further.

[75] Comme l'a expliqué la Cour d'appel de la Colombie-Britannique dans l'arrêt *Dunlop c. B.C. Hydro & Power Authority* (1988), 32 B.C.L.R. (2d) 334, p. 338-339, il y a trois raisons principales pour lesquelles cette distinction est importante. Premièrement, il existe des difficultés liées à la complexité d'une condition implicite prévoyant le versement du salaire en lieu et place d'un préavis, et à la question de savoir s'il est facile de dégager implicitement une telle condition d'un contrat de travail. Deuxièmement, le fait de dégager l'existence d'une telle condition implicite [TRADUCTION] « signifierait que, si un employeur choisissait de verser le salaire au lieu de donner un préavis, il respecterait alors le contrat et ne le violerait pas », et, pour cette raison, « le contrat exigerait le plein paiement du salaire immédiatement ». Troisièmement, si l'employeur choisissait d'appliquer une telle condition implicite et ne donnait pas de préavis de cessation d'emploi, [TRADUCTION] « l'employé ne serait pas tenu de limiter son préjudice en cherchant un autre emploi », étant donné que cette condition requiert le plein paiement du salaire sans égard aux pertes réelles subies par l'employé. Il est donc important que les tribunaux et les parties comprennent bien cette distinction, car elle peut affecter profondément la situation financière des employés. Dans la mesure où certaines décisions suggèrent le contraire, je dois, avec égards, exprimer mon désaccord.

[76] Enfin, à cette étape de l'analyse, il peut également être opportun, dans certains cas, de se demander si les clauses visant à limiter ou supprimer le droit que confère la common law à un employé ont été adéquatement portées à son attention (*Paquette*, par. 18; *Taggart*, par. 20-23; *Poole c. Whirlpool Corp.*, 2011 ONCA 808, 97 C.C.E.L. (3d) 20, par. 5-6). Toutefois, cette question ne se soulève pas en l'espèce. De plus, comme l'ont fait remarquer plusieurs intervenants dans le cadre du présent pourvoi, il peut être approprié de se demander si la clause en litige est compatible avec les normes d'emploi minimales (*Machtinger*, p. 1004). Cette question n'a pas été examinée par les juridictions inférieures et, dans les circonstances de l'espèce, il n'est pas nécessaire de s'y attarder davantage.

[77] In sum, I agree with the trial judge that Mr. Matthews is entitled to receive damages equal to what he would have received pursuant to the LTIP, subject to mitigation.

(2) Good Faith

[78] Again, and I say so respectfully, the parties' arguments on good faith were confounding when placed side by side. Mr. Matthews focused largely on the duty of honest performance, and confirmed at the hearing that he is not seeking damages for mental distress flowing from a breach of the duty to exercise good faith in the manner of dismissal, noting that this "just doesn't get him there" in respect of the LTIP (transcript, at p. 17). Ocean, in contrast, defended the conclusion of the Court of Appeal that there was "no bad faith" in "the manner in which [Mr. Matthews] was treated", recalling specifically the trial judge's finding that Mr. Matthews had failed to show that Ocean had planned to terminate him in order to deprive him of his LTIP entitlement (see para. 122).

[79] Ocean is no doubt correct on this very last point. That said, and contrary to the succinct conclusion of the majority judges in the Court of Appeal, I share Mr. Matthews' view that the trial judge did make abundantly clear that the treatment experienced by Mr. Matthews from 2007 until the moment of his departure constituted dishonest conduct on the part of Ocean. He found, as a matter of fact, that Ocean's senior manager undertook a four-year "campaign", characterized by lies and dishonesty, to push Mr. Matthews out of operations (see, e.g., paras. 294, 296, 298 and 301).

[80] The trial judge did not, however, explicitly find a breach of contract resulting from this dishonesty.

[77] En résumé, je suis d'accord avec le juge de première instance pour conclure que M. Matthews a droit à des dommages-intérêts correspondant au paiement qu'il aurait reçu en vertu du RILT, déduction faite des sommes découlant de l'atténuation des dommages.

(2) Bonne foi

[78] Une fois de plus, je tiens à souligner, toujours avec égards, que les arguments des parties sur la bonne foi étaient déroutants lorsque considérés côte à côte. En effet, M. Matthews s'est essentiellement attaché à l'obligation d'exécution honnête, et il a confirmé, lors de l'audience, qu'il ne réclame pas de dommages-intérêts pour les souffrances morales susceptibles de découler d'un manquement à l'obligation d'agir de bonne foi dans la façon de procéder à un congédiement, faisant remarquer que cela [TRADUCTION] « ne le rapproche tout simplement pas de son objectif » en ce qui concerne le RILT (transcription, p. 17). Ocean, quant à elle, a défendu la conclusion de la Cour d'appel selon laquelle [TRADUCTION] « la manière dont [M. Matthews] avait été traité » n'avait été entachée d'« aucune mauvaise foi », rappelant précisément la conclusion du juge de première instance portant que M. Matthews n'avait pas été en mesure d'établir qu'Ocean avait planifié son renvoi afin de le priver de son droit au paiement prévu par le RILT (voir par. 122).

[79] Il ne fait aucun doute qu'Ocean a raison sur ce tout dernier point. Cela dit, contrairement à la conclusion succincte des juges majoritaires de la Cour d'appel, je partage l'opinion de M. Matthews selon laquelle le juge de première instance a très clairement indiqué que la façon dont il a été traité de 2007 jusqu'au moment de son départ constituait une conduite malhonnête de la part d'Ocean. Le juge a tiré une conclusion de fait portant que le cadre supérieur d'Ocean avait mené pendant quatre ans une « campagne » afin d'écarter M. Matthews des opérations et que cette période avait été marquée par la malhonnêteté et le mensonge (voir, p. ex., par. 294, 296, 298 et 301).

[80] Le juge de première instance n'a toutefois pas conclu explicitement que cette malhonnêteté avait

He did not speak to the duty of honest performance, likely because — given that the original pleadings were filed before *Bhasin*'s release — *Bhasin* was not pleaded at trial. Nor did he pursue an analysis, in accordance with *Wallace* and *Keays*, to determine whether this dishonesty amounted to a breach of the duty to exercise good faith in the manner of dismissal. One suspects this too reflected the character of the pleadings, since no compensatory damages for mental distress flowing from Mr. Matthews' treatment in the manner of his dismissal were pursued.

[81] On this latter point, I would take this opportunity to recall that, had the issue been properly placed before the trial judge, it was certainly within the trial judge's prerogative to tie the dishonesty that occurred over the four-year period to the "manner of dismissal". Due to the circumstances in *Wallace* and *Keays*, "in the manner of dismissal" was originally conceptualized as the *moment* of dismissal, suggesting to some degree that good faith must exist only at the very end of the employment relationship. Yet, circumstances of constructive dismissal show that this reading sometimes needs to be extended. Following *Potter*, an employee's constructive dismissal may be better understood as the consequence of conduct over a series of events in time, and not just a tipping point. On this reading, *Potter* extends the notion of "in the manner of dismissal" to encompass circumstances in which termination stems from an employee's decision to leave their job brought about, as here, by a series of events that predate the actual moment of the parting of ways between employer and employee (paras. 31-35). The constructive dismissal may, depending on the facts of a given case, reflect a choice to leave prompted by a series of changes to the employee's working conditions over time, absent any misconduct. Or a constructive dismissal may reflect a choice to leave where dishonest or like misconduct eventually pushes the employee out the door. In the latter circumstance, this suggests that, at least retrospectively, the duty is relevant to the performance of the contract prior to the moment of termination.

entraîné une violation du contrat. Il n'a pas traité de l'obligation d'exécution honnête, vraisemblablement parce que — comme les premiers actes de procédure ont été déposés avant que l'arrêt *Bhasin* ne soit rendu — cette décision n'a pas été plaidée au procès. Le juge de première instance n'a pas non plus procédé, sur la base des arrêts *Wallace* et *Keays*, à une analyse en vue de déterminer si cette conduite malhonnête constituait un manquement à l'obligation d'agir de bonne foi dans la façon de procéder au congédiement. On peut supposer que cela découle de la teneur des actes de procédure, en ce qu'aucune demande de dommages-intérêts compensatoires n'a été présentée pour les souffrances morales découlant du traitement réservé à M. Matthews par suite de la façon dont il a été congédié.

[81] Relativement à ce dernier point, je profite de l'occasion pour rappeler que, si la question avait été soumise adéquatement au juge de première instance, il lui aurait certes été loisible de rattacher les gestes malhonnêtes survenus au cours de la période de quatre ans aux « circonstances du congédiement ». Compte tenu des circonstances dans lesquelles les arrêts *Wallace* et *Keays* ont été rendus, l'expression « circonstances du congédiement » a initialement été interprétée comme visant le *moment* du congédiement, ce qui tendait dans une certaine mesure à suggérer que la bonne foi était requise uniquement à la toute fin de la relation d'emploi. Or, les situations de congédiement déguisé montrent que cette conception doit parfois être élargie. À la suite de l'arrêt *Potter*, il est sans doute plus juste de considérer le congédiement déguisé d'un employé comme étant la conséquence d'une série d'événements échelonnés dans le temps plutôt que comme un seul et unique moment décisif. D'après cette interprétation, l'arrêt *Potter* élargit la notion de « circonstances du congédiement » aux situations où une cessation d'emploi découle de la décision d'un employé de quitter son emploi en raison d'une suite d'événements survenus avant le moment concret où la relation employeur-employé a été rompue, comme c'est le cas en l'espèce (par. 31-35). Il peut arriver que, selon les faits propres à une affaire donnée, le congédiement déguisé reflète la décision d'un employé de quitter son emploi en raison de nombreuses modifications apportées aux conditions de son emploi au fil du

Indeed, there is no coherent reason why the measure of misconduct cannot be understood retrospectively in cases of wrongful dismissal "so long as it is 'a component of the manner of dismissal'" (*Doyle v. Zochem Inc.*, 2017 ONCA 130, 31 C.C.P.B. (2nd) 200, at para. 13, citing *Gismondi v. Toronto (City)* (2003), 64 O.R. (3d) 688 (C.A.), at para. 23).

[82] In recognizing this, *Potter* affirmed what courts were already doing: examining the employment relationship retrospectively, and thus implicitly finding that good faith is owed not merely at the very end of the relationship. As Professor England has observed, courts have frequently examined whether employers treated their employees with good faith in constructive dismissal cases by, for example, ensuring employees were safeguarded from bullying, intimidation, and harassment from managers and other employers (*Individual Employment Law* (2nd ed. 2008), at pp. 92-93). This extension in *Potter* thus allowed for a more flexible measure of conduct over the period leading up to the moment of actual termination of the employment contract.[4]

[83] I would not, however, say anything further on how *Bhasin*, on the one hand, and *Wallace* and *Keays*, on the other, apply to this case. It suffices to say that a contractual breach of good faith rests on a wholly distinct basis from that relating to the failure to provide reasonable notice. I say this on the basis of my proposed conclusion above, with respect to Mr. Matthews' financial claim for breach

[4] See C. Mummé, "*Bhasin v. Hrynew*: A New Era for Good Faith in Canadian Employment Law, or Just Tinkering at the Margins?" (2016), 32 *Int'l J. Comp. Lab. L. & Ind. Rel.* 117, at p. 122.

temps, sans qu'il y ait eu de conduite répréhensible. Par ailleurs, un congédiement déguisé peut également refléter la décision d'un employé de quitter son travail lorsqu'une conduite malhonnête ou une autre action répréhensible l'a finalement poussé à le faire. Dans ce dernier cas, on pourrait croire que, rétrospectivement à tout le moins, l'obligation s'applique à l'exécution du contrat avant sa résiliation. De fait, il n'existe aucune raison cohérente pour que la conduite répréhensible ne puisse pas être considérée rétrospectivement dans les affaires de congédiement injustifié, [TRADUCTION] « pourvu qu'elle constitue un "aspect des circonstances du congédiement" » de l'employé (*Doyle c. Zochem Inc.*, 2017 ONCA 130, 31 C.C.P.B. (2nd) 200, par. 13, citant *Gismondi c. Toronto (City)* (2003), 64 O.R. (3d) 688 (C.A.), par. 23).

[82] En reconnaissant ceci dans l'arrêt *Potter*, la Cour a confirmé ce que les tribunaux faisaient déjà, en ce qu'ils examinaient la relation d'emploi de façon rétrospective et concluaient ainsi implicitement que l'obligation d'agir de bonne foi ne s'applique pas uniquement à la toute fin de la relation. Comme l'a fait observer le professeur England, les tribunaux sont souvent appelés à se demander, dans les cas de congédiement déguisé, si les employeurs ont traité leurs employés de bonne foi, par exemple en veillant à ce que ceux-ci ne soient pas victimes d'intimidation ou de harcèlement de la part de gestionnaires ou de collègues (*Individual Employment Law* (2e éd. 2008), p. 92-93). Cet élargissement dans Potter des principes applicables a donc accordé plus de souplesse en étendant l'appréciation de la conduite à la période précédant le moment concret où le contrat de travail a été résilié[4].

[83] Je ne me prononcerai toutefois pas davantage sur la manière dont l'arrêt *Bhasin*, d'une part, et les arrêts *Wallace* et *Keays*, d'autre part, s'appliquent à la présente espèce. Qu'il suffise de dire qu'un manquement à l'obligation contractuelle d'agir de bonne foi repose sur des fondements entièrement distincts de ceux liés à l'omission de donner un préavis raisonnable. J'affirme cela en m'appuyant

[4] Voir C. Mummé, « *Bhasin v. Hrynew* : A New Era for Good Faith in Canadian Employment Law, or Just Tinkering at the Margins? » (2016), 32 *Int'l J. Comp. Lab. L. & Ind. Rel.* 117, p. 122.

of the implied duty to provide reasonable notice. At the hearing, counsel for Mr. Matthews acknowledged that, if he received damages to compensate him for his lost LTIP payment as part of his reasonable notice damages, he cannot now claim the same amount under the *Hadley* principle. While the breaches of contract are indeed distinct, they cannot be deployed to provide what amounts to double recovery. Moreover, Mr. Matthews drew the Court's attention to the anxiety caused by Ocean, but made no request for damages for mental distress. As noted, while he originally claimed for punitive damages at trial, he did not pursue this head of damages on appeal. Given that Mr. Matthews failed to press his claim with further detail or argument, even when questioned on point by members of the Court, I need not go further to decide whether some duty of good faith has been breached, since no further remedies are being sought.

sur la conclusion que j'ai proposée précédemment à l'égard de la demande de réparation pécuniaire présentée par M. Matthews pour manquement à l'obligation tacite de donner un préavis raisonnable. À l'audience, l'avocat de M. Matthews a reconnu que, si les dommages-intérêts qui sont accordés à ce dernier pour l'absence de préavis raisonnable incluent des dommages-intérêts le compensant pour la perte du paiement prévu par le RILT, M. Matthews ne saurait réclamer maintenant ce même paiement suivant le principe établi dans l'arrêt *Hadley*. Bien qu'il s'agisse de violations de contrat distinctes, elles ne peuvent être appliquées pour accorder une réparation qui équivaudrait à une double indemnité. Qui plus est, si M. Matthews a attiré l'attention de notre Cour sur l'angoisse causée par Ocean, il n'a pas demandé de dommages-intérêts pour souffrances morales. Comme il a été mentionné plus tôt, quoique M. Matthews ait initialement réclamé des dommages-intérêts punitifs au procès, il n'a pas fait valoir ce chef de réclamation en appel. Étant donné que M. Matthews n'a pas fourni de détails ou d'arguments supplémentaires à cet égard, même lorsqu'il a été interrogé sur ce point par des juges de notre Cour, il n'est pas nécessaire que je m'y attarde davantage pour décider s'il y a eu manquement à une obligation de bonne foi, aucune réparation additionnelle n'étant réclamée.

[84] Further, I note that Mr. Matthews and several interveners argue that the general organizing principle of good faith described in *Bhasin* manifests itself in various ways throughout the whole of the contractual performance. Ocean answers that any extension of good faith would be an unwieldy precedent.

[84] De plus, je souligne que M. Matthews et plusieurs intervenants prétendent que le principe directeur général de bonne foi décrit dans l'arrêt *Bhasin* se manifeste de diverses façons tout au long de l'exécution du contrat. Pour sa part, Ocean affirme que tout élargissement de l'obligation de bonne foi créerait un précédent peu facile à appliquer.

[85] Mr. Matthews' argument is a serious one. Not all mistreatment by an employer will result in a constructive dismissal — some employees, for financial or other reasons, might choose not to leave their job. It might be that, as argued by various parties in this appeal, a duty of good faith will one day bind the employer based on a mutual obligation of loyalty in a non-fiduciary sense during the life of the employment contract, owed reciprocally by both the employer and employee. I recognize, however, that

[85] L'argument de M. Matthews est important. Le traitement incorrect réservé à un employé par son employeur ne se traduit pas dans tous les cas par un congédiement déguisé — il peut arriver que, pour des raisons financières ou autres, l'employé concerné décide de ne pas quitter son emploi. Il se pourrait, comme l'ont soutenu diverses parties au présent pourvoi, que les employeurs soient un jour tenus pendant la durée du contrat de travail à un devoir de bonne foi basé sur une obligation mutuelle

whether the law should recognize this is a matter of fair debate.

[86] This is a dismissal case. In light of the comment in *Bhasin* (at para. 40) that the common law should develop in an incremental fashion, I would decline to decide whether a broader duty exists during the life of the employment contract in the absence of an appropriate factual record.

[87] Lastly, I recall that in his original application, Mr. Matthews sought a declaration that the termination of his employment reflected conduct on the part of Ocean that was oppressive and unfair, and that his dismissal was "carried out in bad faith at law and in breach of [Ocean's] duty of good faith". I recognize that, generally speaking, the mental distress that an employee might feel as a result of employer dishonesty is translated by law, in financial terms, as damages, and that, further, Mr. Matthews has declined to seek such damages here. Nevertheless, a proper acknowledgment that an employer's conduct was contrary to the expected standard of good faith can transcend the request for damages, and may be meaningful for an employee in a way that a mere finding that reasonable notice was provided cannot. One aspect of this relates to dignity in the workplace, and the non-financial value associated with fair treatment upon dismissal (J. Fudge, "The Limits of Good Faith in the Contract of Employment: From *Addis* to *Vorvis* to *Wallace* and Back Again?" (2007), 32 *Queen's L.J.* 529, at p. 548; G. Anderson, D. Brodie and J. Riley, *The Common Law Employment Relationship: A Comparative Study* (2017), at ch. 11). Indeed, this Court has been emphatic in recognizing that, in addition to whatever financial dimension work entails, a person's employment is "an essential component of [their] sense of identity, self-worth and emotional well-being" (*Reference re Public Service Employee Relations Act (Alta.)*, [1987] 1 S.C.R. 313, at p. 368). To this end, it is understandable that employees seek some recognition that they have been mistreated, reflecting that they feel it unfair, beyond

de loyauté, au sens non fiduciaire de ce terme, devoir liant réciproquement l'employeur et l'employé. Je reconnais toutefois que la question de savoir si ce principe devrait être reconnu en droit suscite des débats légitimes.

[86] Il s'agit en l'espèce d'une affaire de congédiement. Compte tenu de l'observation formulée dans l'arrêt *Bhasin* (par. 40) selon laquelle la common law doit évoluer de manière progressive, je m'abstiens, en l'absence d'un dossier factuel adéquat, de me prononcer sur l'existence d'une obligation de portée plus large pendant la durée du contrat de travail.

[87] Enfin, je rappelle que, dans sa demande initiale, M. Matthews sollicitait une déclaration indiquant que la cessation de son emploi résultait de la conduite abusive et injuste d'Ocean à son endroit, et que son congédiement avait été [TRADUCTION] « effectué de mauvaise foi au sens de la loi et en contravention à l'obligation [d'Ocean] d'agir de bonne foi ». Je reconnais que, de manière générale, les souffrances morales que pourrait éprouver un employé en raison de la conduite malhonnête de l'employeur se traduisent en droit, sur le plan financier, par des dommages-intérêts, et que, en outre, M. Matthews s'est abstenu de réclamer de tels dommages-intérêts en l'espèce. Néanmoins, une reconnaissance formelle que la conduite d'un employeur a contrevenu à la norme de la bonne foi attendue peut transcender la présentation d'une demande en dommages-intérêts, et pourrait avoir pour l'employé concerné une valeur significative que ne saurait avoir à ses yeux une simple conclusion qu'un préavis raisonnable a été donné. Cela découle notamment de la dignité à laquelle aspirent les employés au sein de leur milieu de travail et de la valeur non financière qu'ils associent au fait d'être traités équitablement en cas de congédiement (J. Fudge, « The Limits of Good Faith in the Contract of Employment : From *Addis* to *Vorvis* to *Wallace* and Back Again? » (2007), 32 *Queen's L.J.* 529, p. 548; G. Anderson, D. Brodie et J. Riley, *The Common Law Employment Relationship : A Comparative Study* (2017), ch. 11). D'ailleurs, notre Cour a clairement reconnu qu'en plus de la dimension financière qu'il présente, l'emploi est « une composante essentielle du sens de l'identité d'une

any compensatory matter, that they were forced to quit in such circumstances.

[88] Regrettably, Mr. Matthews gave no explanation as to what basis this Court would make a formal declaration in these circumstances. I would refrain from making a declaration of a contractual breach related to good faith in the formal sense. Nonetheless, I would observe that it is clear from the findings at trial Mr. Matthews was mistreated and lied to about the security of his future with the company in the years leading up to his constructive dismissal in a manner that contributed to making his job intolerable. Compensation during the reasonable notice period does not speak to this. While it may not result in further remedies in this case, it is not inappropriate to recall that the "non-monetary benefit" (*Potter*, at para. 84) derived from the performance of work can be wrongly taken from employees if, at dismissal, they are lied to or misled as to the reasons for termination.

V. Conclusion

[89] For the foregoing reasons, I would allow the appeal, set aside the judgment of the Court of Appeal and restore the judgment of the Supreme Court of Nova Scotia, with costs throughout.

Appeal allowed with costs throughout.

Solicitors for the appellant: Levitt, Toronto; Mitchell & Ferguson, Associates, Halifax.

personne, de sa valorisation et de son bien-être sur le plan émotionnel » (*Renvoi relatif à la Public Service Employee Relations Act (Alb.)*, [1987] 1 R.C.S. 313, p. 368). Pour cette raison, il est compréhensible que des employés demandent qu'on reconnaisse qu'ils ont été traités de façon incorrecte, ce qui reflète le fait qu'ils estiment injuste, indépendamment des aspects financiers d'une telle situation, d'avoir été forcés de quitter leur emploi en pareilles circonstances.

[88] Malheureusement, M. Matthews n'a pas expliqué sur quel fondement notre Cour devrait s'appuyer pour prononcer une déclaration formelle dans les présentes circonstances. Je m'abstiendrais donc de prononcer formellement une déclaration portant qu'il y a eu manquement à l'obligation contractuelle d'agir de bonne foi. Je ferais néanmoins observer qu'il ressort clairement des conclusions tirées au procès que M. Matthews a été traité de façon incorrecte et qu'on lui a menti à l'égard de sa sécurité d'emploi future dans l'entreprise au cours des années ayant précédé son congédiement déguisé, et ce, d'une manière qui a contribué à créer une situation intolérable pour lui au travail. La rémunération versée pendant la période de préavis raisonnable ne tient pas compte de cela. Bien que l'observation susmentionnée ne se traduise pas par une réparation additionnelle en l'espèce, il n'est pas inapproprié de rappeler que « l'avantage non pécuniaire » (*Potter*, par. 84) qu'un salarié tire de l'exécution de son travail peut lui être retiré injustement si, en cas de congédiement, on lui ment et on le trompe quant aux raisons pour lesquelles on met fin à son emploi.

V. Conclusion

[89] Pour les motifs qui précèdent, je suis d'avis d'accueillir le pourvoi, d'écarter l'arrêt de la Cour d'appel et de rétablir le jugement de la Cour suprême de la Nouvelle-Écosse, le tout avec dépens devant toutes les cours.

Pourvoi accueilli avec dépens dans toutes les cours.

Procureurs de l'appelant : Levitt, Toronto; Mitchell & Ferguson, Associates, Halifax.

Solicitors for the respondent: Barteaux Durnford, Halifax.

Solicitors for the intervener the Canadian Association for Non-Organized Employees: Ball Professional Corporation, Toronto; CSuite Law, Toronto; SJO Legal Professional Corporation, Toronto.

Solicitors for the intervener Don Valley Community Legal Services: Monkhouse Law, Toronto.

Solicitors for the intervener the Law Students' Legal Advice Program: Tevlin Gleadle Curtis Employment Law Strategies, Vancouver.

Solicitors for the intervener the Canadian Association of Counsel to Employers: McCarthy Tétrault, Toronto.

Solicitors for the intervener Parkdale Community Legal Services: Nelligan O'Brien Payne, Ottawa; Parkdale Community Legal Services, Toronto.

Procureurs de l'intimée : Barteaux Durnford, Halifax.

Procureurs de l'intervenante Canadian Association for Non-Organized Employees : Ball Professional Corporation, Toronto; CSuite Law, Toronto; SJO Legal Professional Corporation, Toronto.

Procureurs de l'intervenant Don Valley Community Legal Services : Monkhouse Law, Toronto.

Procureurs de l'intervenant Law Students' Legal Advice Program : Tevlin Gleadle Curtis Employment Law Strategies, Vancouver.

Procureurs de l'intervenante l'Association canadienne des avocats d'employeurs : McCarthy Tétrault, Toronto.

Procureurs de l'intervenant Parkdale Community Legal Services : Nelligan O'Brien Payne, Ottawa; Parkdale Community Legal Services, Toronto.

TAB 8

Her Majesty The Queen in Right of the Province of Newfoundland and Labrador *Appellant*

v.

AbitibiBowater Inc., Abitibi-Consolidated Inc., Bowater Canadian Holdings Inc., Ad Hoc Committee of Bondholders, Ad Hoc Committee of Senior Secured Noteholders and U.S. Bank National Association (Indenture Trustee for the Senior Secured Noteholders) *Respondents*

and

Attorney General of Canada, Attorney General of Ontario, Attorney General of British Columbia, Attorney General of Alberta, Her Majesty The Queen in Right of British Columbia, Ernst & Young Inc., as Monitor, and Friends of the Earth Canada *Interveners*

Indexed as: Newfoundland and Labrador *v.* AbitibiBowater Inc.

2012 SCC 67

File No.: 33797.

2011: November 16; 2012: December 7.

Present: McLachlin C.J. and LeBel, Deschamps, Fish, Abella, Rothstein, Cromwell, Moldaver and Karakatsanis JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR QUEBEC

Bankruptcy and Insolvency — Provable claims — Contingent claims — Corporation filing for insolvency protection — Province issuing environmental protection orders against corporation and seeking declaration that orders not "claims" under Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36 ("CCAA"), and not subject to claims procedure order — Whether environmental protection orders are monetary claims that

Sa Majesté la Reine du chef de la province de Terre-Neuve-et-Labrador *Appelante*

c.

AbitibiBowater Inc., Abitibi-Consolidated Inc., Bowater Canadian Holdings Inc., comité ad hoc des créanciers obligataires, comité ad hoc des porteurs de billets garantis de premier rang et U.S. Bank National Association (fiduciaire désigné par l'acte constitutif pour les porteurs de billets garantis de premier rang) *Intimés*

et

Procureur général du Canada, procureur général de l'Ontario, procureur général de la Colombie-Britannique, procureur général de l'Alberta, Sa Majesté la Reine du chef de la Colombie-Britannique, Ernst & Young Inc., en sa qualité de contrôleur, et Les Ami(e)s de la Terre Canada *Intervenants*

Répertorié : Terre-Neuve-et-Labrador *c.* AbitibiBowater Inc.

2012 CSC 67

N^o^ du greffe : 33797.

2011 : 16 novembre; 2012 : 7 décembre.

Présents : La juge en chef McLachlin et les juges LeBel, Deschamps, Fish, Abella, Rothstein, Cromwell, Moldaver et Karakatsanis.

EN APPEL DE LA COUR D'APPEL DU QUÉBEC

Faillite et insolvabilité — Réclamations prouvables — Réclamations éventuelles — Demande de protection contre l'insolvabilité par une société — Ordonnances environnementales émises par la province contre la société et demande, par la province, d'un jugement déclarant que les ordonnances ne constituent pas des « réclamations » aux termes de la Loi sur les arrangements avec les créanciers des compagnies, L.R.C. 1985,

can be compromised in corporate restructuring under CCAA — Whether CCAA is ultra vires or constitutionally inapplicable by permitting court to determine whether environmental order is a monetary claim.

A was involved in industrial activity in Newfoundland and Labrador (the "Province"). In a period of general financial distress, it ended its last operation there, filed for insolvency protection in the United States and obtained a stay of proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). The Province subsequently issued five orders under the *Environmental Protection Act*, S.N.L. 2002, c. E-14.2, requiring A to submit remediation action plans for five industrial sites it had occupied, three of which had been expropriated by the Province, and to complete the remediation actions. The Province also brought a motion for a declaration that a claims procedure order issued under the *CCAA* in relation to A's proposed reorganization did not bar the Province from enforcing the environmental protection orders. The Province argued that the environmental protection orders were not "claims" under the *CCAA* and therefore could not be stayed and subject to a claims procedure order. It further argued that Parliament lacked the constitutional competence under its power to make laws in relation to bankruptcy and insolvency to stay orders that were validly made in the exercise of a provincial power. A contested the motion, arguing that the orders were monetary in nature and hence fell within the definition of the word "claim" in the claims procedure order. The *CCAA* court dismissed the Province's motion. The Court of Appeal denied the Province leave to appeal.

Held (McLachlin C.J. and LeBel J. dissenting): The appeal should be dismissed.

Per Deschamps, Fish, Abella, Rothstein, Cromwell, Moldaver and Karakatsanis JJ.: Not all orders issued by regulatory bodies are monetary in nature and thus provable claims in an insolvency proceeding, but some may be, even if the amounts involved are not quantified

ch. C-36 (« LACC »), et qu'elles ne sont pas assujetties à l'ordonnance relative à la procédure de réclamations — Les ordonnances environnementales constituent-elles des réclamations pécuniaires pouvant faire l'objet d'une transaction dans le cadre d'une restructuration sous le régime de la LACC? — La LACC est-elle ultra vires ou constitutionnellement inapplicable en permettant au tribunal de déterminer si une ordonnance environnementale constitue une réclamation pécuniaire?

A a poursuivi des activités industrielles à Terre-Neuve-et-Labrador (la « province »). Dans une période de grandes difficultés financières, elle a mis un terme à ses activités dans la province, elle a présenté une demande de protection contre l'insolvabilité aux États-Unis et elle a obtenu une suspension des procédures en vertu de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, ch. C-36 (« *LACC* »). La province a par la suite prononcé cinq ordonnances environnementales en vertu de l'*Environmental Protection Act*, S.N.L. 2002, ch. E-14.2, contraignant A à présenter des plans de restauration pour cinq sites industriels qu'elle avait occupés, dont trois avaient été expropriés par la province, et à réaliser les plans de restauration approuvés. La province a également demandé par requête un jugement déclarant qu'une ordonnance relative à la procédure de réclamations rendue aux termes de la *LACC* dans le cadre de la réorganisation proposée de A n'empêchait pas la province d'exécuter les ordonnances environnementales. La province a plaidé que les ordonnances environnementales ne constituent pas des « réclamations » au sens de la *LACC* et que leur exécution ne peut donc être suspendue ni être assujettie à une ordonnance relative à la procédure de réclamations. Elle a de plus fait valoir que le pouvoir du Parlement de légiférer en matière de faillite et d'insolvabilité ne lui confère pas la compétence constitutionnelle pour suspendre l'application des ordonnances prononcées dans l'exercice valide de pouvoirs provinciaux. A a contesté la requête et a soutenu que les ordonnances étaient de nature pécuniaire et qu'elles étaient donc visées par la définition du terme « réclamation » utilisé dans l'ordonnance relative à la procédure de réclamations. Le juge chargé d'appliquer la *LACC* a rejeté la requête de la province et la Cour d'appel a rejeté la demande d'autorisation d'appel de la province.

Arrêt (la juge en chef McLachlin et le juge LeBel sont dissidents) : Le pourvoi est rejeté.

Les juges Deschamps, Fish, Abella, Rothstein, Cromwell, Moldaver et Karakatsanis : Les ordonnances des organismes administratifs ne sont pas toutes de nature pécuniaire, et donc des réclamations prouvables dans le cadre de procédures d'insolvabilité, mais

at the outset of the proceedings. In the environmental context, the *CCAA* court must determine whether there are sufficient facts indicating the existence of an environmental duty that will ripen into a financial liability owed to the regulatory body that issued the order. In such a case, the relevant question is not simply whether the body has formally exercised its power to claim a debt. A *CCAA* court does not assess claims or orders on the basis of form alone. If the order is not framed in monetary terms, the *CCAA* court must determine, in light of the factual matrix and the applicable statutory framework, whether it is a claim that will be subject to the claims process.

There are three requirements orders must meet in order to be considered claims that may be subject to the insolvency process in a case such as the one at bar. First, there must be a debt, a liability or an obligation to a creditor. In this case, the first criterion was met because the Province had identified itself as a creditor by resorting to environmental protection enforcement mechanisms. Second, the debt, liability or obligation must be incurred as of a specific time. This requirement was also met since the environmental damage had occurred before the time of the *CCAA* proceedings. Third, it must be possible to attach a monetary value to the debt, liability or obligation. The present case turns on this third requirement, and the question is whether orders that are not expressed in monetary terms can be translated into such terms.

A claim may be asserted in insolvency proceedings even if it is contingent on an event that has not yet occurred. The criterion used by courts to determine whether a contingent claim will be included in the insolvency process is whether the event that has not yet occurred is too remote or speculative. In the context of an environmental protection order, this means that there must be sufficient indications that the regulatory body that triggered the enforcement mechanism will ultimately perform remediation work and assert a monetary claim. If there is sufficient certainty in this regard, the court will conclude that the order can be subject to the insolvency process.

certaines peuvent l'être en dépit du fait qu'elles ne sont pas quantifiées dès le début des procédures. En matière environnementale, le tribunal chargé de l'application de la *LACC* doit déterminer s'il y a suffisamment de faits indiquant qu'il existe une obligation environnementale de laquelle résultera une dette envers l'organisme administratif qui a prononcé l'ordonnance. En pareil cas, la question pertinente ne se résume pas à déterminer si l'organisme a formellement exercé son pouvoir de réclamer une dette. Le tribunal qui évalue une réclamation ou une ordonnance ne se limite pas à un examen de sa forme. Si l'ordonnance n'est pas formulée en termes pécuniaires, le tribunal doit déterminer, en fonction des faits en cause et du cadre législatif applicable, si elle constitue une réclamation qui sera assujettie au processus de réclamation.

Pour qu'elles constituent des réclamations pouvant être assujetties au processus applicable en matière d'insolvabilité dans une affaire telle celle en l'espèce, les ordonnances doivent satisfaire à trois conditions. Premièrement, il doit s'agir d'une dette, d'un engagement ou d'une obligation envers un créancier. En l'espèce, il a été satisfait à la première condition puisque la province s'est présentée comme créancière en ayant recours aux mécanismes d'application en matière de protection de l'environnement. Deuxièmement, la dette, l'engagement ou l'obligation doit avoir pris naissance à un moment précis. Il a également été satisfait à cette condition puisque les dommages environnementaux sont survenus avant que les procédures en vertu de la *LACC* ne soient entamées. Troisièmement, il doit être possible d'attribuer une valeur pécuniaire à cette dette, cet engagement ou cette obligation. La présente affaire est centrée sur cette troisième condition, et la question est de savoir si des ordonnances qui ne sont pas formulées en termes pécuniaires peuvent être formulées en de tels termes.

Il est possible de faire valoir une réclamation dans le cadre de procédures d'insolvabilité même si elle dépend d'un événement non encore survenu. Le critère retenu par les tribunaux pour décider si une réclamation éventuelle sera incluse dans le processus d'insolvabilité est celui qui consiste à déterminer si l'événement non encore survenu est trop éloigné ou conjectural. Dans le contexte d'une ordonnance environnementale, cela signifie qu'il doit y avoir des indications suffisantes permettant de conclure que l'organisme administratif qui a eu recours aux mécanismes d'application de la loi effectuera en fin de compte des travaux de décontamination et présentera une réclamation pécuniaire. Si cela est suffisamment certain, le tribunal conclura que l'ordonnance peut être assujettie au processus d'insolvabilité.

Certain indicators can guide the *CCAA* court in this assessment, including whether the activities are ongoing, whether the debtor is in control of the property, and whether the debtor has the means to comply with the order. The court may also consider the effect that requiring the debtor to comply with the order would have on the insolvency process. The analysis is grounded in the facts of each case. In this case, the *CCAA* court's assessment of the facts, particularly its finding that the orders were the first step towards performance of the remediation work by the Province, leads to no conclusion other than that it was sufficiently certain that the Province would perform remediation work and therefore fall within the definition of a creditor with a monetary claim.

Subjecting such orders to the claims process does not extinguish the debtor's environmental obligations any more than subjecting any creditor's claim to that process extinguishes the debtor's obligation to pay a debt. It merely ensures that the Province's claim will be paid in accordance with insolvency legislation. Full compliance with orders that are found to be monetary in nature would shift the costs of remediation to third party creditors and replace the polluter-pay principle with a "third-party-pay" principle. Moreover, to subject environmental protection orders to the claims process is not to invite corporations to restructure in order to rid themselves of their environmental liabilities. Reorganization made necessary by insolvency is hardly ever a deliberate choice, and when the risks corporations engage in materialize, the dire costs are borne by almost all stakeholders.

Because the provisions on the assessment of claims in insolvency matters relate directly to Parliament's jurisdiction, the ancillary powers doctrine is not relevant to this case. The interjurisdictional immunity doctrine is also inapplicable, because a finding that a claim of an environmental creditor is monetary in nature does not interfere in any way with the creditor's activities; its claim is simply subject to the insolvency process.

Per McLachlin C.J. (dissenting): Remediation orders made under a province's environmental protection

Certains indicateurs permettent de guider le tribunal dans cette analyse, notamment si les activités se poursuivent, si le débiteur exerce un contrôle sur le bien et s'il dispose des moyens de se conformer à l'ordonnance. Il est également possible pour le tribunal de prendre en compte les conséquences qu'entraînerait sur le processus d'insolvabilité le fait d'exiger du débiteur qu'il se conforme à l'ordonnance. L'analyse est fondée sur les faits propres à chaque cas. En l'espèce, l'appréciation des faits par le tribunal, plus particulièrement sa constatation que les ordonnances constituaient la première étape en vue de la décontamination des sites par la province, ne permet de tirer aucune conclusion autre que celle suivant laquelle il était suffisamment certain que la province exécuterait des travaux de décontamination et qu'elle était par conséquent visée par la définition d'un créancier ayant une réclamation pécuniaire.

Le fait d'assujettir ces ordonnances au processus de réclamations n'éteint pas les obligations environnementales qui incombent au débiteur, pas plus que le fait de soumettre à ce processus les réclamations des créanciers n'éteint l'obligation du débiteur de payer ses dettes. Le fait d'assujettir une ordonnance au processus de réclamation vise simplement à faire en sorte que le paiement au créancier sera fait conformément aux dispositions législatives applicables en matière d'insolvabilité. Le respect intégral des ordonnances dont la nature pécuniaire est reconnue transférerait le coût de la décontamination aux tiers créanciers et substituerait au principe du pollueur-payeur celui du « tiers-payeur ». En outre, l'assujettissement des ordonnances environnementales à la procédure de réclamations n'équivaut pas à convier les sociétés à se réorganiser dans le but d'échapper à leurs obligations environnementales. Une réorganisation rendue nécessaire par l'insolvabilité de la société peut difficilement être assimilée à un choix délibéré, et lorsque les risques auxquels s'exposent les sociétés se concrétisent, la quasi-totalité des personnes ayant des intérêts dans la société en supportent les terribles coûts.

L'application de la doctrine des pouvoirs accessoires n'est pas pertinente en l'espèce car les dispositions régissant l'évaluation des réclamations en matière d'insolvabilité sont directement reliées à la compétence du législateur fédéral. La doctrine de la protection des compétences exclusives ne s'applique pas non plus parce qu'une conclusion selon laquelle un créancier œuvrant dans le domaine de l'environnement détient une réclamation pécuniaire ne modifie en rien les activités de ce créancier; sa réclamation est simplement assujettie au processus d'insolvabilité.

La juge en chef McLachlin (dissidente) : Les ordonnances exigeant la décontamination émises aux termes

legislation impose ongoing regulatory obligations on the corporation required to clean up the pollution. They may only be reduced to monetary claims which can be compromised under *CCAA* proceedings in narrow circumstances where a province has done the remediation work, or where it is "sufficiently certain" that it will do the work. This last situation is regulated by the provisions of the *CCAA* for contingent or future claims. The test is whether there is a likelihood approaching certainty that the province will do the work. "Likelihood approaching certainty" recognizes that the government's decision is discretionary and may be influenced by competing political and social considerations, which are not normally subject to judicial consideration. Insofar as this determination touches on the division of powers, I am in substantial agreement with Deschamps J.

Apart from the orders related to the work done or tendered for on the Buchans property, the orders for remediation in this case are not claims that can be compromised. The *CCAA* maintains the fundamental distinction between regulatory obligations under the general law aimed at the protection of the public and monetary claims that can be compromised in *CCAA* restructuring or bankruptcy. The *CCAA* judge never asked himself the critical question of whether it was "sufficiently certain" that the Province would do the work itself. His failure to consider that question requires this Court to answer it in his stead. There is nothing on the record to support the view that the Province will move to remediate the properties. It has not been shown that the contamination poses immediate health risks which must be addressed without delay. It has not been shown that the Province has taken any steps to do any work. And it has not been shown that the Province has set aside or even contemplated setting aside money for this work. The Province retained a number of options, including leaving the sites contaminated, or calling on Abitibi to remediate following its emergence from restructuring. There is nothing in the record that makes it more probable, much less establishes "sufficient certainty", that the Province will opt to do the work itself.

d'une loi provinciale sur la protection de l'environnement imposent des exigences réglementaires continues à la personne morale requise de remédier à la pollution. Ces ordonnances ne peuvent être converties en réclamations pécuniaires pouvant faire l'objet de transactions dans le cadre de procédures engagées aux termes de la *LACC* que dans certaines circonstances particulières, lorsqu'une province a exécuté les travaux ou lorsqu'il est « suffisamment certain » qu'elle exécutera les travaux. Cette deuxième situation est prévue par les dispositions de la *LACC* relatives aux réclamations éventuelles ou futures. Le critère consiste à déterminer s'il existe une probabilité proche de la certitude que la province exécutera les travaux. Une « probabilité proche de la certitude » reconnaît que la décision du gouvernement est discrétionnaire et peut être influencée par des considérations politiques et sociales concurrentes qui sont normalement soustraites à l'examen judiciaire. Dans la mesure où cette décision touche le partage des pouvoirs, je souscris pour l'essentiel à l'opinion exprimée par la juge Deschamps.

À l'exception des ordonnances relatives aux travaux sur le site de Buchans déjà exécutés ou à l'égard desquels des appels d'offres ont été lancés, les ordonnances exigeant la décontamination en l'espèce ne constituent pas des réclamations pouvant faire l'objet de transactions dans le cadre d'une restructuration. La *LACC* établit une distinction fondamentale entre les exigences réglementaires découlant d'une loi d'application générale visant la protection du public, d'une part, et les réclamations pécuniaires pouvant faire l'objet d'une transaction dans le cadre d'une restructuration engagée sous le régime de la *LACC* ou en matière de faillite, d'autre part. Le juge de première instance ne s'est jamais posé la question cruciale de savoir s'il était « suffisamment certain » que la province exécuterait elle-même les travaux. Le fait qu'il n'ait pas examiné cette question oblige notre Cour à y répondre à sa place. Aucune preuve au dossier ne laisse croire que la province entreprendra la décontamination des sites. Il n'a pas été démontré que la contamination pose pour la santé des risques immédiats exigeant la prise de mesures dans les plus brefs délais. Il n'a pas été démontré que la province a pris quelque mesure que ce soit pour réaliser des travaux. Et il n'a pas été démontré que la province a prévu des sommes d'argent pour ces travaux ou qu'elle a même songé à en prévoir. La province a conservé un certain nombre de choix, notamment laisser les sites contaminés, ou demander à Abitibi d'exécuter les travaux lorsqu'elle aura complété sa restructuration. Rien au dossier n'indique qu'il est plus probable, et encore moins qu'il est « suffisamment certain », que la province choisira d'exécuter elle-même la décontamination.

Per LeBel J. (dissenting): The test proposed by the Chief Justice according to which the evidence must show that there is a "likelihood approaching certainty" that the Province would remediate the contamination itself is not the established test for determining where and how a contingent claim can be liquidated in bankruptcy and insolvency law. The test of "sufficient certainty" described by Deschamps J. best reflects how both the common law and the civil law view and deal with contingent claims. Applying that test, the appeal should be allowed on the basis that there is no evidence that the Province intends to perform the remedial work itself.

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By Deschamps J.

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By McLachlin C.J. (dissenting)

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Le juge LeBel (dissident) : Le critère que propose la Juge en chef, selon lequel la preuve doit démontrer une « probabilité proche de la certitude » que la province se chargerait de la décontamination, ne constitue pas le critère établi pour déterminer si, et de quelle façon, une réclamation éventuelle peut être liquidée en droit de la faillite et de l'insolvabilité. Le critère de ce qui est « suffisamment certain » qu'énonce la juge Deschamps reflète mieux la façon dont la common law et le droit civil envisagent et traitent les réclamations éventuelles. En appliquant ce critère, il y aurait lieu d'accueillir le pourvoi puisqu'aucune preuve ne confirme l'intention de la province d'exécuter elle-même les travaux de décontamination.

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David R. Wingfield, *Paul D. Guy* and *Philip Osborne*, for the appellant.

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David R. Wingfield, *Paul D. Guy* et *Philip Osborne*, pour l'appelante.

Sean F. Dunphy, *Nicholas McHaffie*, *Joseph Reynaud* and *Marc B. Barbeau*, for the respondents.

Christopher Rupar and *Marianne Zoric*, for the intervener the Attorney General of Canada.

Josh Hunter, *Robin K. Basu*, *Leonard Marsello* and *Mario Faieta*, for the intervener the Attorney General of Ontario.

R. Richard M. Butler, for the intervener the Attorney General of British Columbia.

Roderick Wiltshire, for the intervener the Attorney General of Alberta.

Elizabeth J. Rowbotham, for the intervener Her Majesty The Queen in Right of British Columbia.

Robert I. Thornton, *John T. Porter* and *Rachelle F. Moncur*, for the intervener Ernst & Young Inc., as Monitor.

William A. Amos, *Anastasia M. Lintner*, *Hugh S. Wilkins* and *R. Graham Phoenix*, for the intervener the Friends of the Earth Canada.

The judgment of Deschamps, Fish, Abella, Rothstein, Cromwell, Moldaver and Karakatsanis JJ. was delivered by

[1] DESCHAMPS J. — The question in this appeal is whether orders issued by a regulatory body with respect to environmental remediation work can be treated as monetary claims under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*").

[2] Regulatory bodies may become involved in reorganization proceedings when they order the debtor to comply with statutory rules. As a matter of principle, reorganization does not amount to a licence to disregard rules. Yet there are circumstances in which valid and enforceable orders will be subject to an arrangement under the *CCAA*. One such circumstance is where a regulatory body

Sean F. Dunphy, *Nicholas McHaffie*, *Joseph Reynaud* et *Marc B. Barbeau*, pour les intimés.

Christopher Rupar et *Marianne Zoric*, pour l'intervenant le procureur général du Canada.

Josh Hunter, *Robin K. Basu*, *Leonard Marsello* et *Mario Faieta*, pour l'intervenant le procureur général de l'Ontario.

R. Richard M. Butler, pour l'intervenant le procureur général de la Colombie-Britannique.

Roderick Wiltshire, pour l'intervenant le procureur général de l'Alberta.

Elizabeth J. Rowbotham, pour l'intervenante Sa Majesté la Reine du chef de la Colombie-Britannique.

Robert I. Thornton, *John T. Porter* et *Rachelle F. Moncur*, pour l'intervenante Ernst & Young Inc., en sa qualité de contrôleur.

William A. Amos, *Anastasia M. Lintner*, *Hugh S. Wilkins* et *R. Graham Phoenix*, pour l'intervenant Les Ami(e)s de la Terre Canada.

Version française du jugement des juges Deschamps, Fish, Abella, Rothstein, Cromwell, Moldaver et Karakatsanis rendu par

[1] LA JUGE DESCHAMPS — La question soulevée dans le présent pourvoi est de savoir si des ordonnances d'un organisme administratif relatives à des travaux de décontamination peuvent être traitées comme des réclamations pécuniaires aux termes de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, ch. C-36 (« *LACC* »).

[2] Un organisme administratif peut être appelé à intervenir dans le cadre de procédures de réorganisation lorsqu'il prononce une ordonnance intimant au débiteur de se conformer à une règle prescrite par la loi. En principe, une réorganisation ne permet pas à une personne d'ignorer ses obligations légales. Par ailleurs, en certaines circonstances, une ordonnance valable et exécutoire sera assujettie

makes an environmental order that explicitly asserts a monetary claim.

[3] In other circumstances, it is less clear whether an order can be treated as a monetary claim. The appellant and a number of interveners posit that an order issued by an environmental body is not a claim under the *CCAA* if the order does not require the debtor to make a payment. I agree that not all orders issued by regulatory bodies are monetary in nature and thus provable claims in an insolvency proceeding, but some may be, even if the amounts involved are not quantified at the outset of the proceeding. In the environmental context, the *CCAA* court must determine whether there are sufficient facts indicating the existence of an environmental duty that will ripen into a financial liability owed to the regulatory body that issued the order. In such a case, the relevant question is not simply whether the body has formally exercised its power to claim a debt. A *CCAA* court does not assess claims — or orders — on the basis of form alone. If the order is not framed in monetary terms, the court must determine, in light of the factual matrix and the applicable statutory framework, whether it is a claim that will be subject to the claims process.

[4] The case at bar concerns contamination that occurred, prior to the *CCAA* proceedings, on property that is largely no longer under the debtor's possession and control. The *CCAA* court found on the facts of this case that the orders issued by Her Majesty the Queen in right of the Province of Newfoundland and Labrador ("Province") were simply a first step towards remediating the contaminated property and asserting a claim for the resulting costs. In the words of the *CCAA* court, "the intended, practical and realistic effect of the EPA Orders was to establish a basis for the Province to

à un arrangement conclu en vertu de la *LACC*. C'est le cas notamment lorsqu'un organisme administratif prononce une ordonnance environnementale qui est explicitement formulée en termes pécuniaires.

[3] En d'autres circonstances, il est plus difficile de savoir si une ordonnance peut être traitée comme une réclamation pécuniaire. L'appelante et certains des intervenants affirment qu'une ordonnance émise par un organisme de protection de l'environnement ne constitue pas une réclamation au sens de la *LACC* si elle n'exige pas du débiteur qu'il lui paye un montant d'argent. Je conviens que les ordonnances des organismes administratifs ne constituent pas toutes des réclamations pécuniaires, et donc des réclamations prouvables dans le cadre de procédures d'insolvabilité, mais certaines peuvent l'être en dépit du fait qu'elles ne sont pas quantifiées dès le début des procédures. En matière environnementale, le tribunal chargé de l'application de la *LACC* doit déterminer s'il y a suffisamment de faits indiquant qu'il existe une obligation environnementale de laquelle résultera une dette envers l'organisme administratif qui a prononcé l'ordonnance. En pareil cas, la question pertinente ne se résume pas à déterminer si l'organisme a formellement exercé son pouvoir de réclamer une dette. Lorsque le tribunal évalue une réclamation (ou une ordonnance) il ne se limite pas à un examen de sa forme. Si l'ordonnance n'est pas formulée en termes pécuniaires, le tribunal doit déterminer, en fonction des faits en cause et du cadre législatif applicable, si elle constitue une réclamation qui sera assujettie au processus de réclamation.

[4] Le présent pourvoi a trait à des dommages environnementaux survenus avant que les procédures sous le régime de la *LACC* ne soient engagées, des dommages causés à des terrains qui, en majeure partie, ne sont plus en la possession du débiteur ni sous son contrôle. Le tribunal de première instance a conclu, selon les faits en l'espèce, que les ordonnances émises par Sa Majesté la Reine du chef de la province de Terre-Neuve-et-Labrador (« province ») ne constituaient que la première étape en vue de restaurer les sites contaminés et de réclamer les coûts engagés. Comme l'a exprimé le juge de

recover amounts of money to be eventually used for the remediation of the properties in question" (2010 QCCS 1261, 68 C.B.R. (5th) 1, at para. 211). As a result, the *CCAA* court found that the orders were clearly monetary in nature. I see no error of law and no reason to interfere with this finding of fact. I would dismiss the appeal with costs.

I. Facts and Procedural History

[5] For over 100 years, AbitibiBowater Inc. and its affiliated or predecessor companies (together, "Abitibi") were involved in industrial activity in Newfoundland and Labrador. In 2008, Abitibi announced the closure of a mill that was its last operation in that province.

[6] Within two weeks of the announcement, the Province passed the *Abitibi-Consolidated Rights and Assets Act*, S.N.L. 2008, c. A-1.01 ("*Abitibi Act*"), which immediately transferred most of Abitibi's property in Newfoundland and Labrador to the Province and denied Abitibi any legal remedy for this expropriation.

[7] The closure of its mill in Newfoundland and Labrador was one of many decisions Abitibi made in a period of general financial distress affecting its activities both in the United States and in Canada. It filed for insolvency protection in the United States on April 16, 2009. It also sought a stay of proceedings under the *CCAA* in the Superior Court of Quebec, as its Canadian head office was located in Montréal. The *CCAA* stay was ordered on April 17, 2009.

[8] In the same month, Abitibi also filed a notice of intent to submit a claim to arbitration under NAFTA (the *North American Free Trade Agreement Between the Government of Canada, the Government of the United Mexican States and the Government of the United States of America*,

première instance, [TRADUCTION] « les ordonnances avaient pour effet attendu, pratique et réaliste d'établir le fondement d'une réclamation permettant à la province de récupérer des sommes d'argent qui seraient utilisées pour procéder aux travaux de décontamination » (2010 QCCS 1261, 68 C.B.R. (5th) 1, par. 211). Par conséquent, pour le tribunal, les ordonnances étaient clairement de nature pécuniaire. Je ne vois aucune erreur de droit ni aucune raison de modifier ces conclusions de fait. Je suis d'avis de rejeter le pourvoi avec dépens.

I. Faits et historique judiciaire

[5] Pendant plus d'une centaine d'années, AbitibiBowater Inc., et ses auteurs ou sociétés filiales (ensemble, « Abitibi ») ont poursuivi des activités industrielles à Terre-Neuve-et-Labrador. En 2008, Abitibi a annoncé la fermeture de la dernière des scieries qu'elle exploitait dans cette province.

[6] Dans les deux semaines qui ont suivi cette annonce, la province a adopté l'*Abitibi-Consolidated Rights and Assets Act*, S.N.L. 2008, ch. A-1.01 (« *Abitibi Act* »), qui transférait immédiatement à la province la plus grande partie des biens d'Abitibi situés à Terre-Neuve-et-Labrador et privait la société de tous recours judiciaires en relation avec cette expropriation.

[7] La fermeture de sa scierie à Terre-Neuve-et-Labrador est l'une des nombreuses décisions prises par Abitibi dans une période où de grandes difficultés financières touchaient ses activités au Canada et aux États-Unis. Le 16 avril 2009, elle a présenté une demande de protection contre l'insolvabilité aux États-Unis. Elle a également demandé à la Cour supérieure du Québec, à Montréal, où elle a son siège social au Canada, une suspension des procédures en vertu de la *LACC*. La suspension a été ordonnée le 17 avril 2009.

[8] Au cours du même mois, Abitibi a aussi déposé un avis d'intention de soumettre une plainte à l'arbitrage en vertu de l'ALENA (*Accord de libre-échange nord-américain entre le gouvernement du Canada, le gouvernement des États-Unis d'Amérique et le gouvernement des États-Unis du Mexique*,

Can. T.S. 1994 No. 2) for losses resulting from the *Abitibi Act*, which, according to Abitibi, exceeded $300 million.

[9] On November 12, 2009, the Province's Minister of Environment and Conservation ("Minister") issued five orders (the "*EPA* Orders") under s. 99 of the *Environmental Protection Act*, S.N.L. 2002, c. E-14.2 ("*EPA*"). The *EPA* Orders required Abitibi to submit remediation action plans to the Minister for five industrial sites, three of which had been expropriated, and to complete the approved remediation actions. The *CCAA* judge estimated the cost of implementing these plans to be from "the mid-to-high eight figures" to "several times higher" (para. 81).

[10] On the day it issued the *EPA* Orders, the Province brought a motion for a declaration that a claims procedure order issued under the *CCAA* in relation to Abitibi's proposed reorganization did not bar the Province from enforcing the *EPA* Orders. The Province argued — and still argues — that non-monetary statutory obligations are not "claims" under the *CCAA* and hence cannot be stayed and be subject to a claims procedure order. It further submits that Parliament lacks the constitutional competence under its power to make laws in relation to bankruptcy and insolvency to stay orders that are validly made in the exercise of a provincial power.

[11] Abitibi contested the motion and sought a declaration that the *EPA* Orders were stayed and that they were subject to the claims procedure order. It argued that the *EPA* Orders were monetary in nature and hence fell within the definition of the word "claim" in the claims procedure order.

R.T. Can. 1994 n^{o} 2) relativement à des pertes découlant de l'application de l'*Abitibi Act*, lesquelles totalisaient, selon Abitibi, une somme supérieure à 300 millions de dollars.

[9] Le 12 novembre 2009, le ministre provincial de l'Environnement et de la Conservation (« ministre ») a prononcé, en vertu de l'art. 99 de l'*Environmental Protection Act*, S.N.L. 2002, ch. E-14.2 (« *EPA* »), cinq ordonnances (les « ordonnances *EPA* ») contraignant Abitibi à présenter au ministre des plans de restauration pour cinq sites industriels, dont trois avaient été expropriés, et à réaliser les plans de restauration approuvés. Le juge chargé de l'instance instituée sous le régime de la *LACC* a évalué les coûts de la mise en œuvre de ces plans à une somme se situant [TRADUCTION] « entre cinquante et cent millions de dollars », ou « plusieurs fois plus élevée » (par. 81).

[10] Le jour même où elle émettait les ordonnances *EPA*, la province a demandé par requête un jugement déclarant qu'une ordonnance relative à la procédure de réclamations rendue aux termes de la *LACC* dans le cadre de la réorganisation proposée d'Abitibi n'empêchait pas la province d'exécuter les ordonnances *EPA*. La province a soutenu — et soutient toujours — que des obligations légales de nature non pécuniaire ne constituent pas des « réclamations » au sens de la *LACC* et que leur exécution ne peut donc être suspendue ni être assujettie à une ordonnance relative à la procédure de réclamations. Elle fait de plus valoir que le pouvoir du Parlement de légiférer en matière de faillite et d'insolvabilité ne lui confère pas la compétence constitutionnelle pour suspendre l'application des ordonnances prononcées dans l'exercice valide de pouvoirs provinciaux.

[11] Abitibi a contesté la requête et a demandé un jugement déclarant que les ordonnances *EPA* avaient été suspendues et qu'elles étaient assujetties à l'ordonnance relative à la procédure de réclamations. Abitibi a soutenu que les ordonnances *EPA* étaient de nature pécuniaire et qu'elles étaient donc visées par la définition du terme « réclamation » utilisé dans l'ordonnance relative à la procédure de réclamations.

[12] Gascon J. of the Quebec Superior Court, sitting as a *CCAA* court, dismissed the Province's motion. He found that he had the authority to characterize the orders as "claims" if the underlying regulatory obligations "remain[ed], in a particular fact pattern, truly financial and monetary in nature" (para. 148). He declared that the *EPA* Orders were stayed by the initial stay order and were not subject to the exception found in that order. He also declared that the filing by the Province of any claim based on the *EPA* Orders was subject to the claims procedure order, and reserved to the Province the right to request an extension of time to assert a claim under the claims procedure order and to Abitibi the right to contest such a request.

[12] Le juge Gascon de la Cour supérieure du Québec, siégeant aux termes de la *LACC*, a rejeté la requête de la province. Il a statué qu'il avait le pouvoir de qualifier les ordonnances de « réclamations » si les obligations légales sous-jacentes [TRADUCTION] « demeur[aient], dans une situation factuelle particulière, de nature véritablement financière et pécuniaire » (par. 148). Il a déclaré que les ordonnances *EPA* avaient été suspendues en vertu de l'ordonnance de suspension initiale et qu'elles n'étaient pas visées par l'exception énoncée dans cette ordonnance. Il a également déclaré que la présentation, par la province, de toute réclamation fondée sur les ordonnances *EPA* était assujettie à l'ordonnance relative à la procédure de réclamations; il a réservé à la province le droit de demander par requête une prorogation du délai pour présenter une réclamation en vertu de la procédure de réclamations et a confirmé le droit d'Abitibi de contester une telle requête.

[13] In the Court of Appeal, Chamberland J.A. denied the Province leave to appeal (2010 QCCA 965, 68 C.B.R. (5th) 57). In his view, the appeal had no reasonable chance of success, because Gascon J. had found as a fact that the *EPA* Orders were financial or monetary in nature. Chamberland J.A. also found that no constitutional issue arose, given that the Superior Court judge had merely characterized the orders in the context of the restructuring process; the judgment did not "'immunise' Abitibi from compliance with the EPA Orders" (para. 33). Finally, he noted that Gascon J. had reserved the Province's right to request an extension of time to file a claim in the *CCAA* process.

[13] En Cour d'appel, le juge Chamberland a rejeté la demande d'autorisation d'appel présentée par la province (2010 QCCA 965, 68 C.B.R. (5th) 57). À son avis, l'appel n'avait aucune chance raisonnable de succès parce que le juge Gascon avait conclu, comme question de faits, que les ordonnances *EPA* étaient de nature financière ou pécuniaire. Le juge Chamberland a également estimé qu'aucune question constitutionnelle ne se posait, car le juge de la Cour supérieure n'avait fait que qualifier les ordonnances dans le contexte du processus de restructuration; le jugement ne [TRADUCTION] « "soustrayait" pas Abitibi à son obligation de se conformer aux ordonnances *EPA* » (par. 33). Enfin, il a fait remarquer que le juge Gascon avait réservé à la province le droit de demander la prorogation de délai pour produire une réclamation en vertu de la *LACC*.

II. Positions of the Parties

II. Thèses des parties

[14] The Province argues that the *CCAA* court erred in interpreting the relevant *CCAA* provisions in a way that nullified the *EPA*, and that the interpretation is inconsistent with both the ancillary powers doctrine and the doctrine of interjurisdictional immunity. The Province further submits

[14] La province soutient que le tribunal de première instance a commis l'erreur d'interpréter les dispositions applicables de la *LACC* de façon à invalider l'*EPA* et que cette interprétation est incompatible tant avec la doctrine des pouvoirs accessoires qu'avec celle de la protection des compétences

that, in any event, the *EPA* Orders are not "claims" within the meaning of the *CCAA*. It takes the position that "any plan of compromise and arrangement that Abitibi might submit for court approval must make provision for compliance with the *EPA* Orders" (A.F., at para. 32).

[15] Abitibi contends that the factual record does not provide a basis for applying the constitutional doctrines. It relies on the *CCAA* court's findings of fact, particularly the finding that the Province's intent was to establish the basis for a monetary claim. Abitibi submits that the true issue is whether a province that has a monetary claim against an insolvent company can obtain a preference against other unsecured creditors by exercising its regulatory power.

III. Constitutional Questions

[16] At the Province's request, the Chief Justice stated the following constitutional questions:

1. Is the definition of "claim" in s. 2(1) of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, *ultra vires* the Parliament of Canada or constitutionally inapplicable to the extent this definition includes statutory duties to which the debtor is subject pursuant to s. 99 of the *Environmental Protection Act*, S.N.L. 2002, c. E-14.2?

2. Is s. 11 of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, *ultra vires* the Parliament of Canada or constitutionally inapplicable to the extent this section gives courts jurisdiction to bar or extinguish statutory duties to which the debtor is subject pursuant to s. 99 of the *Environmental Protection Act*, S.N.L. 2002, c. E-14.2?

3. Is s. 11 of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, *ultra vires* the Parliament of Canada or constitutionally inapplicable to the extent this section gives courts jurisdiction to

exclusives. La province fait de plus valoir que, de toute façon, les ordonnances *EPA* ne constituent pas des « réclamations » au sens de la *LACC*. Elle soutient que [TRADUCTION] « tout plan de transaction et d'arrangement qu'Abitibi pourrait soumettre à l'approbation du tribunal doit prévoir qu'[Abitibi] doit se conformer aux ordonnances *EPA* » (m.a., par. 32).

[15] Abitibi soutient que l'application des doctrines constitutionnelles ne trouve aucun fondement dans les faits du dossier. Elle appuie sa position sur les conclusions de fait tirées par le tribunal de première instance, plus particulièrement celles où le tribunal conclut que l'intention de la province était d'établir le fondement d'une réclamation pécuniaire. Abitibi plaide que la véritable question est de savoir si, par l'exercice de son pouvoir de réglementation, une province ayant une réclamation pécuniaire à faire valoir contre une entreprise insolvable peut obtenir une préférence à l'encontre d'autres créanciers non garantis.

III. Questions constitutionnelles

[16] À la demande de la province, la Juge en chef a formulé les questions constitutionnelles suivantes :

1. La définition d'une « réclamation » énoncée au par. 2(1) de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, ch. C-36, outrepasse-t-elle les pouvoirs du Parlement du Canada ou est-elle constitutionnellement inapplicable dans la mesure où elle englobe les obligations légales auxquelles le débiteur est assujetti en application de l'art. 99 de l'*Environmental Protection Act*, S.N.L. 2002, ch. E-14.2?

2. L'article 11 de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, ch. C-36, outrepasse-t-il les pouvoirs du Parlement du Canada ou est-il constitutionnellement inapplicable dans la mesure où il confère aux tribunaux la compétence pour libérer le débiteur des obligations légales auxquelles il est ou pourrait être assujetti en application de l'art. 99 de l'*Environmental Protection Act*, S.N.L. 2002, ch. E-14.2?

3. L'article 11 de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, ch. C-36, outrepasse-t-il les pouvoirs du Parlement du Canada ou est-il constitutionnellement inapplicable dans la mesure

review the exercise of ministerial discretion under s. 99 of the *Environmental Protection Act*, S.N.L. 2002, c. E-14.2?

[17] I note that the question whether a *CCAA* court has constitutional jurisdiction to stay a provincial order that is *not* a monetary claim does not arise here, because the stay order in this case did not affect non-monetary orders. However, the question may arise in other cases. In 2007, Parliament expressly gave *CCAA* courts the power to stay regulatory orders that are not monetary claims by amending the *CCAA* to include the current version of s. 11.1(3) (*An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act, the Wage Earner Protection Program Act and chapter 47 of the Statutes of Canada, 2005*, S.C. 2007, c. 36, s. 65) (the "2007 amendments"). Thus, future cases may give courts the opportunity to consider the question raised by the Province in an appropriate factual context. The only constitutional question that needs to be answered in this case concerns the jurisdiction of a *CCAA* court to determine whether an environmental order that is not framed in monetary terms is in fact a monetary claim.

[18] Processing creditors' claims against an insolvent debtor in an equitable and orderly manner is at the heart of insolvency legislation, which falls under a head of power attributed to Parliament. Rules concerning the assessment of creditors' claims, such as the determination of whether a creditor has a monetary claim, relate directly to the equitable and orderly treatment of creditors in an insolvency process. There is no need to perform a detailed analysis of the pith and substance of the provisions on the assessment of claims in insolvency matters to conclude that the federal legislation governing the characterization of an order as a monetary claim is valid. Because the provisions relate directly to Parliament's jurisdiction,

où il confère aux tribunaux la compétence pour réviser l'exercice du pouvoir discrétionnaire conféré au ministre par l'art. 99 de l'*Environmental Protection Act*, S.N.L. 2002, ch. E-14.2?

[17] Je souligne que la question de savoir si, aux termes de la *LACC*, un tribunal a compétence constitutionnelle pour suspendre l'application d'une ordonnance provinciale qui *ne* constitue *pas* une réclamation pécuniaire ne se pose pas en l'espèce parce que l'ordonnance de suspension en cause ne visait pas ces ordonnances. La question pourrait toutefois se poser dans d'autres affaires. En 2007, par l'ajout du par. 11.1(3) de la *LACC*, le législateur fédéral a explicitement conféré aux tribunaux compétents aux termes de la *LACC* le pouvoir de suspendre l'application des ordonnances d'un organisme administratif qui ne constituent pas des réclamations pécuniaires (*Loi modifiant la Loi sur la faillite et l'insolvabilité, la Loi sur les arrangements avec les créanciers des compagnies, la Loi sur le Programme de protection des salariés et le chapitre 47 des Lois du Canada (2005)*, L.C. 2007, ch. 36, art. 65) (les « modifications de 2007 »). Ainsi, les tribunaux auront l'occasion d'analyser la question soulevée par la province lorsque le contexte factuel s'y prêtera. La seule question constitutionnelle qui requiert une réponse en l'espèce a trait à la compétence d'un tribunal, aux termes de la *LACC*, de déterminer si une ordonnance environnementale qui n'est pas formulée en termes pécuniaires constitue, en fait, une réclamation pécuniaire.

[18] Le traitement équitable et ordonné des réclamations présentées par des créanciers contre un débiteur insolvable se situe au cœur même de la législation en matière d'insolvabilité, un domaine de compétence attribué au législateur fédéral. L'établissement de règles relatives à l'évaluation des réclamations des créanciers, comme celle permettant de déterminer si un créancier fait valoir une réclamation pécuniaire, concerne directement le traitement équitable et ordonné des créanciers dans le cadre d'un processus établi en matière d'insolvabilité. Il n'est pas nécessaire d'analyser en détail le caractère véritable des dispositions régissant l'évaluation des réclamations en matière d'insolvabilité pour conclure à la validité du texte législatif fédéral

the ancillary powers doctrine is not relevant to this case. I also find that the interjurisdictional immunity doctrine is not applicable. A finding that a claim of an environmental creditor is monetary in nature does not interfere in any way with the creditor's activities. Its claim is simply subjected to the insolvency process.

[19] What the Province is actually arguing is that courts should consider the form of an order rather than its substance. I see no reason why the Province's choice of order should not be scrutinized to determine whether the form chosen is consistent with the order's true purpose as revealed by the Province's own actions. If the Province's actions indicate that, in substance, it is asserting a provable claim within the meaning of federal legislation, then that claim can be subjected to the insolvency process. Environmental claims do not have a higher priority than is provided for in the *CCAA*. Considering substance over form prevents a regulatory body from artificially creating a priority higher than the one conferred on the claim by federal legislation. This Court recognized long ago that a province cannot disturb the priority scheme established by the federal insolvency legislation (*Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453). Environmental claims are given a specific, and limited, priority under the *CCAA*. To exempt orders which are in fact monetary claims from the *CCAA* proceedings would amount to conferring upon provinces a priority higher than the one provided for in the *CCAA*.

IV. Claims Under the *CCAA*

[20] Several provisions of the *CCAA* have been amended since Abitibi filed for insolvency

permettant d'établir qu'une ordonnance constitue une réclamation pécuniaire. L'application de la doctrine des pouvoirs accessoires n'est pas pertinente en l'espèce car les dispositions en cause sont directement reliées à la compétence du législateur fédéral. J'estime également que la doctrine de la protection des compétences exclusives ne s'applique pas en l'espèce. Une conclusion selon laquelle un créancier œuvrant dans le domaine de l'environnement détient une réclamation pécuniaire ne modifie en rien les activités de ce créancier. La réclamation de ce dernier est simplement assujettie au processus d'insolvabilité.

[19] Ce que soutient en fait la province, c'est que les tribunaux devraient examiner la forme des ordonnances plutôt que leur substance. Je ne vois aucune raison empêchant l'examen du choix par la province d'un type d'ordonnance donnée afin de déterminer si la forme choisie concorde avec l'objectif véritable qui se dégage des gestes qu'elle a posés. Si ces gestes indiquent qu'elle fait effectivement valoir une réclamation prouvable au sens de la législation fédérale, alors cette réclamation peut être assujettie au processus d'insolvabilité. Les réclamations en matière d'environnement ne bénéficient pas d'un rang supérieur à celui prévu par les dispositions de la *LACC*. Privilégier l'examen de la substance d'une ordonnance plutôt que de sa forme permet d'éviter qu'un organisme administratif obtienne de façon artificielle une priorité de rang supérieure à celle que la législation fédérale attribue à la réclamation. Notre Cour a depuis longtemps reconnu qu'une province ne pouvait perturber les priorités établies par le régime fédéral d'insolvabilité (*Husky Oil Operations Ltd. c. Ministre du Revenu national*, [1995] 3 R.C.S. 453). La *LACC* établit une priorité précise et limitée à l'égard des réclamations en matière environnementale. Le fait de soustraire aux procédures d'insolvabilité les ordonnances qui sont en fait des réclamations pécuniaires équivaudrait à accorder aux provinces une priorité d'un rang supérieur à celui prévu par la *LACC*.

IV. Réclamations sous le régime de la *LACC*

[20] Plusieurs dispositions de la *LACC* ont été modifiées depuis qu'Abitibi a présenté une demande

protection. Except where otherwise indicated, the provisions I refer to are those that were in force when the stay was ordered.

[21] One of the central features of the *CCAA* scheme is the single proceeding model, which ensures that most claims against a debtor are entertained in a single forum. Under this model, the court can stay the enforcement of most claims against the debtor's assets in order to maintain the *status quo* during negotiations with the creditors. When such negotiations are successful, the creditors typically accept less than the full amounts of their claims. Claims have not necessarily accrued or been liquidated at the outset of the insolvency proceeding, and they sometimes have to be assessed in order to determine the monetary value that will be subject to compromise.

[22] Section 12 of the *CCAA* establishes the basic rules for ascertaining whether an order is a claim that may be subjected to the insolvency process:

12. (1) [Definition of "claim"] For the purposes of this Act, "claim" means any indebtedness, liability or obligation of any kind that, if unsecured, would be a debt provable in bankruptcy within the meaning of the *Bankruptcy and Insolvency Act.*

(2) [Determination of amount of claim] For the purposes of this Act, the amount represented by a claim of any secured or unsecured creditor shall be determined as follows:

(*a*) the amount of an unsecured claim shall be the amount

. . .

(iii) in the case of any other company, proof of which might be made under the *Bankruptcy and Insolvency Act*, but if the amount so provable is not admitted by the company, the amount shall be determined by the court on summary application by the company or by the creditor; . . .

de protection contre l'insolvabilité. À moins d'indication contraire de ma part, les dispositions que je cite sont celles qui étaient en vigueur lorsque la suspension des procédures a été ordonnée.

[21] Une des caractéristiques principales du régime créé par la *LACC* est de traiter la presque totalité des réclamations contre un débiteur suivant une procédure unique devant un même tribunal. En vertu de ce modèle, le tribunal peut ordonner la suspension de la plupart des mesures d'exécution engagées contre les actifs du débiteur de façon à maintenir le statu quo durant la négociation avec les créanciers. Lorsque la négociation réussit, les créanciers consentent habituellement à recevoir moins que le plein montant de leurs réclamations, lesquelles ne sont pas nécessairement exigibles ou liquidées dès le début des procédures d'insolvabilité. Ces réclamations doivent parfois être évaluées afin d'établir la valeur pécuniaire qui fera l'objet du compromis.

[22] L'article 12 de la *LACC* énonce les règles de base pour déterminer si une ordonnance constitue une réclamation pouvant être assujettie au processus applicable en matière d'insolvabilité :

12. (1) [Définition de « réclamation »] Pour l'application de la présente loi, « réclamation » s'entend de toute dette, tout engagement ou toute obligation d'un genre quelconque qui, s'il n'était pas garanti, constituerait une dette prouvable en matière de faillite au sens de la *Loi sur la faillite et l'insolvabilité.*

(2) [Détermination du montant de la réclamation] Pour l'application de la présente loi, le montant représenté par une réclamation d'un créancier garanti ou chirographaire est déterminé de la façon suivante :

a) le montant d'une réclamation non garantie est le montant :

. . .

(iii) dans le cas de toute autre compagnie, dont la preuve pourrait être établie en vertu de la *Loi sur la faillite et l'insolvabilité*, mais si le montant ainsi prouvable n'est pas admis par la compagnie, ce montant est déterminé par le tribunal sur demande sommaire par la compagnie ou le créancier;

[23] Section 12 of the *CCAA* refers to the rules of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"). Section 2 of the *BIA* defines a claim provable in bankruptcy:

"claim provable in bankruptcy", "provable claim" or "claim provable" includes any claim or liability provable in proceedings under this Act by a creditor;

[24] This definition is completed by s. 121(1) of the *BIA*:

121. (1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

[25] Sections 121(2) and 135(1.1) of the *BIA* offer additional guidance for the determination of whether an order is a provable claim:

121. . . .

(2) The determination whether a contingent or unliquidated claim is a provable claim and the valuation of such a claim shall be made in accordance with section 135.

135. . . .

(1.1) The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.

[26] These provisions highlight three requirements that are relevant to the case at bar. First, there must be a debt, a liability or an obligation to a *creditor*. Second, the debt, liability or obligation must be incurred *before the debtor becomes bankrupt*. Third, it must be possible to attach a *monetary value* to the debt, liability or obligation. I will examine each of these requirements in turn.

[23] L'article 12 de la *LACC* renvoie aux règles de la *Loi sur la faillite et l'insolvabilité*, L.R.C. 1985, ch. B-3 (« *LFI* »). L'article 2 de la *LFI* définit ainsi une réclamation prouvable en matière de faillite :

« réclamation prouvable en matière de faillite » ou « réclamation prouvable » Toute réclamation ou créance pouvant être prouvée dans des procédures intentées sous l'autorité de la présente loi par un créancier.

[24] Cette définition est complétée par le par. 121(1) de la *LFI* :

121. (1) Toutes créances et tous engagements, présents ou futurs, auxquels le failli est assujetti à la date à laquelle il devient failli, ou auxquels il peut devenir assujetti avant sa libération, en raison d'une obligation contractée antérieurement à cette date, sont réputés des réclamations prouvables dans des procédures entamées en vertu de la présente loi.

[25] Les paragraphes 121(2) et 135(1.1) de la *LFI* donnent des indications additionnelles lorsqu'il s'agit de déterminer si une ordonnance constitue une réclamation prouvable :

121. . . .

(2) La question de savoir si une réclamation éventuelle ou non liquidée constitue une réclamation prouvable et, le cas échéant, son évaluation sont décidées en application de l'article 135.

135. . . .

(1.1) Le syndic décide si une réclamation éventuelle ou non liquidée est une réclamation prouvable et, le cas échéant, il l'évalue; sous réserve des autres dispositions du présent article, la réclamation est dès lors réputée prouvée pour le montant de l'évaluation.

[26] Ces dispositions font ressortir trois conditions pertinentes à la présente affaire. Premièrement, on doit être en présence d'une dette, d'un engagement ou d'une obligation envers un *créancier*. Deuxièmement, la dette, l'engagement ou l'obligation doit avoir pris naissance *avant que le débiteur ne devienne failli*. Troisièmement, il doit être possible d'attribuer une *valeur pécuniaire* à cette dette, cet engagement ou cette obligation. Je vais examiner chacune de ces conditions à tour de rôle.

[27] The *BIA*'s definition of a provable claim, which is incorporated by reference into the *CCAA*, requires the identification of a creditor. Environmental statutes generally provide for the creation of regulatory bodies that are empowered to enforce the obligations the statutes impose. Most environmental regulatory bodies can be creditors in respect of monetary or non-monetary obligations imposed by the relevant statutes. At this first stage of determining whether the regulatory body is a creditor, the question whether the obligation can be translated into monetary terms is not yet relevant. This issue will be broached later. The only determination that has to be made at this point is whether the regulatory body has exercised its enforcement power against a debtor. When it does so, it identifies itself as a creditor, and the requirement of this stage of the analysis is satisfied.

[28] The enquiry into the second requirement is based on s. 121(1) of the *BIA*, which imposes a time limit on claims. A claim must be founded on an obligation that was "incurred before the day on which the bankrupt becomes bankrupt". Because the date when environmental damage occurs is often difficult to ascertain, s. 11.8(9) of the *CCAA* provides more temporal flexibility for environmental claims:

11.8 . . .

(9) A claim against a debtor company for costs of remedying any environmental condition or environmental damage affecting real property of the company shall be a claim under this Act, whether the condition arose or the damage occurred before or after the date on which proceedings under this Act were commenced.

[29] The creditor's claim will be exempt from the single proceeding requirement if the debtor's corresponding obligation has not arisen as of the time limit for inclusion in the insolvency process. This could apply, for example, to a debtor's statutory obligations relating to polluting activities that continue after the reorganization, because in such cases,

[27] La définition de réclamation prouvable établie par la *LFI* et incorporée par renvoi à la *LACC* exige qu'une personne ait qualité de créancier. Les lois régissant l'environnement pourvoient généralement à la création d'un organisme chargé de voir au respect des obligations qui y sont prévues. La plupart des organismes administratifs peuvent agir à titre de créanciers en relation avec les obligations pécuniaires ou non pécuniaires imposées par ces lois. À cette première étape qui consiste à déterminer si un organisme administratif est un créancier, il n'est pas encore pertinent de décider si l'obligation peut être formulée en termes pécuniaires. Cette question sera abordée à un stade ultérieur. À cette étape, la seule question à trancher est de savoir si l'organisme administratif a exercé, à l'encontre d'un débiteur, son pouvoir de faire appliquer la loi. Lorsqu'il le fait, il s'identifie alors comme créancier et la condition de cette étape est espectée.

[28] L'examen de la seconde condition repose sur le par. 121(1) de la *LFI* qui impose que la réclamation ait pris naissance dans un délai donné. Celle-ci doit se fonder sur une obligation « contractée antérieurement à cette date [la date à laquelle le failli devient failli] ». Comme il est souvent difficile d'établir la date à laquelle un dommage lié à l'environnement est survenu, le par. 11.8(9) de la *LACC* prévoit une certaine flexibilité pour ce qui est des réclamations en matière d'environnement :

11.8 . . .

(9) La réclamation pour les frais de réparation du fait ou dommage lié à l'environnement et touchant un bien immeuble de la compagnie débitrice constitue une réclamation, que la date du fait ou dommage soit antérieure ou postérieure à celle où des procédures sont intentées au titre de la présente loi.

[29] La réclamation du créancier sera exemptée de l'exigence découlant de la procédure unique si l'obligation correspondante du débiteur n'a pas pris naissance dans le délai fixé pour que la réclamation soit incluse dans le processus d'insolvabilité. À titre d'exemple, cela pourrait s'appliquer aux obligations que la loi impose à un débiteur concernant

the damage continues to be sustained after the reorganization has been completed.

[30] With respect to the third requirement, that it be possible to attach a monetary value to the obligation, the question is whether orders that are not expressed in monetary terms can be translated into such terms. I note that when a regulatory body claims an amount that is owed at the relevant date, that is, when it frames its order in monetary terms, the court does not need to make this determination, because what is being claimed is an "indebtedness" and therefore clearly falls within the meaning of "claim" as defined in s. 12(1) of the *CCAA*.

[31] However, orders, which are used to address various types of environmental challenges, may come in many forms, including stop, control, preventative, and clean-up orders (D. Saxe, "Trustees' and Receivers' Environmental Liability Update" (1998), 49 C.B.R. (3d) 138, at p. 141). When considering an order that is not framed in monetary terms, courts must look at its substance and apply the rules for the assessment of claims.

[32] Parliament recognized that regulatory bodies sometimes have to perform remediation work (see House of Commons, *Evidence of the Standing Committee on Industry*, No. 16, 2nd Sess., 35th Parl., June 11, 1996). When one does so, its claim with respect to remediation costs is subject to the insolvency process, but the claim is secured by a charge on the contaminated real property and certain other related property and benefits from a priority (s. 11.8(8) *CCAA*). Thus, Parliament struck a balance between the public's interest in enforcing environmental regulations and the interest of third-party creditors in being treated equitably.

ses activités polluantes qui se poursuivent après la réorganisation, parce qu'en pareilles circonstances, des dommages sont encore causés après que la réorganisation ait été complétée.

[30] En ce qui concerne la troisième condition, soit qu'il doit être possible d'attribuer à l'obligation une valeur pécuniaire, la question est de savoir si des ordonnances qui ne sont pas formulées en termes pécuniaires peuvent être formulées en de tels termes. Je souligne que lorsqu'un organisme administratif réclame une somme qui est due à la date pertinente, il formule ainsi son ordonnance en termes pécuniaires. Le tribunal n'a alors aucune détermination à faire à cette étape car ce qui est réclamé est une « dette » et est, par conséquent, clairement visé par la définition d'une « réclamation » prévue au par. 12(1) de la *LACC*.

[31] Toutefois, parce qu'elles sont utilisées pour traiter divers enjeux environnementaux, les ordonnances peuvent se présenter sous plusieurs formes et peuvent viser notamment la cessation ou le contrôle d'une activité, la prévention et la décontamination (D. Saxe, « Trustees' and Receivers' Environnmental Liability Update » (1998), 49 C.B.R. (3d) 138, p. 141). Lorsqu'ils analysent une ordonnance qui n'est pas formulée en des termes pécuniaires, les tribunaux doivent en examiner la substance et appliquer les règles régissant l'évaluation des réclamations.

[32] Le législateur fédéral reconnaît que les organismes administratifs doivent à l'occasion exécuter des travaux de décontamination (voir Chambre des communes, *Témoignages du Comité permanent de l'industrie*, nº 16, 2e sess., 35e lég., 11 juin 1996). En pareil cas, la réclamation relative aux frais de décontamination est assujettie à la procédure de réclamations en matière d'insolvabilité mais elle est garantie par une charge réelle grevant l'immeuble contaminé et certains immeubles connexes et bénéficie d'un rang prioritaire (par. 11.8(8) *LACC*). Ainsi, le législateur a établi un équilibre entre l'intérêt du public à l'égard de l'application de la réglementation environnementale et les intérêts des tiers créanciers qui doivent être traités de façon équitable.

[33] If Parliament had intended that the debtor always satisfy all remediation costs, it would have granted the Crown a priority with respect to the totality of the debtor's assets. In light of the legislative history and the purpose of the reorganization process, the fact that the Crown's priority under s. 11.8(8) of the *CCAA* is limited to the contaminated property and certain related property leads me to conclude that to exempt environmental orders would be inconsistent with the insolvency legislation. As deferential as courts may be to regulatory bodies' actions, they must apply the general rules.

[33] Si le législateur fédéral avait eu l'intention d'obliger le débiteur à supporter dans tous les cas tous les coûts des travaux de décontamination, il aurait accordé à l'État une priorité applicable à la totalité des actifs du débiteur. Compte tenu de l'historique des dispositions législatives et des objectifs du processus de réorganisation, le fait que la priorité de l'État aux termes du par. 11.8(8) de la *LACC* soit limitée au bien contaminé et à certains biens liés m'amène à conclure qu'une exemption à l'égard des ordonnances environnementales serait incompatible avec la législation en matière d'insolvabilité. Aussi respectueux soient-ils des mesures prises par les organismes administratifs, les tribunaux sont tenus d'appliquer les règles générales.

[34] Unlike in proceedings governed by the common law or the civil law, a claim may be asserted in insolvency proceedings even if it is contingent on an event that has not yet occurred (for the common law, see *Canada v. McLarty*, 2008 SCC 26, [2008] 2 S.C.R. 79, at paras. 17-18; for the civil law, see arts. 1497, 1508 and 1513 of the *Civil Code of Québec*, S.Q. 1991, c. 64). Thus, the broad definition of "claim" in the *BIA* includes *contingent* and *future* claims that would be unenforceable at common law or in the civil law. As for unliquidated claims, a *CCAA* court has the same power to assess their amounts as would a court hearing a case in a common law or civil law context.

[34] Contrairement à l'approche qui prévaut dans le contexte des procédures régies par la common law ou le droit civil, il est possible de faire valoir une réclamation dans le cadre de procédures d'insolvabilité même si elle dépend d'un événement non encore survenu (en common law, voir *Canada c. McLarty*, 2008 CSC 26, [2008] 2 R.C.S. 79, par. 17-18; en droit civil, voir les art. 1497, 1508 et 1513 du *Code civil du Québec*, L.Q. 1991, ch. 64). Ainsi, la définition générale de « réclamation » de la *LFI* englobe des réclamations éventuelles et *futures* qui seraient inexécutoires en common law ou en droit civil. En ce qui concerne les réclamations non liquidées, le tribunal chargé de l'application de la *LACC* a le même pouvoir d'évaluer leur montant qu'un tribunal saisi d'une affaire sous le régime de la common law ou du droit civil.

[35] The reason the *BIA* and the *CCAA* include a broad range of claims is to ensure fairness between creditors and finality in the insolvency proceeding for the debtor. In a corporate liquidation process, it is more equitable to allow as many creditors as possible to participate in the process and share in the liquidation proceeds. This makes it possible to include creditors whose claims have not yet matured when the corporate debtor files for bankruptcy, and thus avert a situation in which they would be faced with an inactive debtor that cannot satisfy a judgment. The rationale is slightly different in the context of a corporate proposal or reorganization. In such cases, the broad approach serves not only to

[35] C'est pour assurer l'équité entre les créanciers ainsi que, pour le débiteur, le caractère définitif de la procédure d'insolvabilité que la *LFI* et la *LACC* englobent un large éventail de réclamations. Dans le cadre de la liquidation d'une société, il est plus équitable de permettre au plus grand nombre possible de créanciers de participer au processus et de se partager le produit de la liquidation. Cela permet d'inclure les créanciers dont les réclamations ne sont pas venues à échéance lorsque le débiteur corporatif devient failli, et ainsi éviter que, ayant cessé ses activités, le débiteur ne puisse pas satisfaire à un jugement rendu en leur faveur. L'approche est quelque peu différente dans

ensure fairness between creditors, but also to allow the debtor to make as fresh a start as possible after a proposal or an arrangement is approved.

[36] The criterion used by courts to determine whether a contingent claim will be included in the insolvency process is whether the event that has not yet occurred is too remote or speculative (*Confederation Treasury Services Ltd. (Bankrupt), Re* (1997), 96 O.A.C. 75). In the context of an environmental order, this means that there must be sufficient indications that the regulatory body that triggered the enforcement mechanism will ultimately perform remediation work and assert a monetary claim to have its costs reimbursed. If there is sufficient certainty in this regard, the court will conclude that the order can be subjected to the insolvency process.

[37] The exercise by the *CCAA* court of its jurisdiction to determine whether an order is a provable claim entails a certain scrutiny of the regulatory body's actions. This scrutiny is in some ways similar to judicial review. There is a distinction, however, and it lies in the object of the assessment that the *CCAA* court must make. The *CCAA* court does not review the regulatory body's exercise of discretion. Rather, it inquires into whether the facts indicate that the conditions for inclusion in the claims process are met. For example, if activities at issue are ongoing, the *CCAA* court may well conclude that the order cannot be included in the insolvency process because the activities and resulting damages will continue after the reorganization is completed and hence exceed the time limit for a claim. If, on the other hand, the regulatory body, having no realistic alternative but to perform the remediation work itself, simply delays framing the order as a claim in order to improve its position in relation to other creditors, the *CCAA* court may conclude

le contexte d'une proposition concordataire présentée par une société ou d'une réorganisation. Dans ces cas, l'objectif que sous-tend une interprétation large est non seulement de garantir l'équité entre créanciers, mais aussi de permettre au débiteur de prendre un nouveau départ dans les meilleures conditions possibles à la suite de l'approbation d'une proposition ou d'un arrangement.

[36] Le critère retenu par les tribunaux pour décider si une réclamation éventuelle sera incluse dans le processus d'insolvabilité est celui qui consiste à déterminer si l'événement non encore survenu est trop éloigné ou conjectural (*Confederation Treasury Service Ltd. (Bankrupt), Re* (1997), 96 O.A.C. 75). Dans le contexte d'une ordonnance environnementale, cela signifie qu'il doit y avoir des indications suffisantes permettant de conclure que l'organisme administratif qui a eu recours aux mécanismes d'application de la loi effectuera en fin de compte des travaux de décontamination et présentera une réclamation pécuniaire afin d'obtenir le remboursement de ses débours. Si cela est suffisamment certain, le tribunal conclura que l'ordonnance peut être assujettie au processus d'insolvabilité.

[37] Lorsqu'il détermine si une ordonnance constitue une réclamation prouvable, le tribunal chargé de l'application de la *LACC* doit, dans une certaine mesure, examiner les actes posés par l'organisme administratif. Cet examen se rapproche à certains égards de celui d'un contrôle judiciaire. La différence se situe, toutefois, au niveau de l'objet de l'évaluation que doit faire le tribunal. Son examen ne porte pas sur l'exercice du pouvoir discrétionnaire par l'organisme administratif. Il doit plutôt déterminer si le contexte factuel indique que les conditions requises pour que l'ordonnance soit incluse dans le processus de réclamations sont respectées. Par exemple, si le débiteur continue d'exercer les activités faisant l'objet de l'intervention de l'organisme administratif, il est fort possible que le tribunal conclue que l'ordonnance ne peut être incorporée au processus d'insolvabilité parce que ces activités et les dommages en découlant se poursuivront après la réorganisation et qu'elles excéderont donc le délai prescrit pour la production d'une

that this course of action is inconsistent with the insolvency scheme and decide that the order has to be subject to the claims process. Similarly, if the property is not under the debtor's control and the debtor does not, and realistically will not, have the means to perform the remediation work, the *CCAA* court may conclude that it is sufficiently certain that the regulatory body will have to perform the work.

[38] Certain indicators can thus be identified from the text and the context of the provisions to guide the *CCAA* court in determining whether an order is a provable claim, including whether the activities are ongoing, whether the debtor is in control of the property, and whether the debtor has the means to comply with the order. The *CCAA* court may also consider the effect that requiring the debtor to comply with the order would have on the insolvency process. Since the appropriate analysis is grounded in the facts of each case, these indicators need not all apply, and others may also be relevant.

[39] Having highlighted three requirements for finding a claim to be provable in a *CCAA* process that need to be considered in the case at bar, I must now discuss certain policy arguments raised by the Province and some of the interveners.

[40] These parties argue that treating a regulatory order as a claim in an insolvency proceeding extinguishes the debtor's environmental obligations, thereby undermining the polluter-pay principle discussed by this Court in *Imperial Oil Ltd. v. Quebec (Minister of the Environment)*, 2003 SCC 58, [2003] 2 S.C.R. 624, at para. 24. This objection

réclamation. Par contre, si l'organisme administratif, n'ayant aucune solution réaliste autre que celle d'effectuer lui-même les travaux de décontamination, ne fait que retarder la production d'une réclamation pécuniaire dans le but d'améliorer sa position par rapport à celle des autres créanciers, le tribunal pourrait conclure que cette démarche n'est pas compatible avec le régime d'insolvabilité et décider que l'ordonnance doit être traitée dans le cadre du processus de réclamations. De même, si le débiteur n'exerce aucun contrôle sur le bien et ne dispose pas, ni ne disposera, de façon réaliste, des moyens pour effectuer les travaux de décontamination, le tribunal pourrait conclure de façon suffisamment certaine que l'organisme administratif devra exécuter les travaux.

[38] Il est ainsi possible de discerner, grâce au libellé des dispositions et à leur contexte, certains indicateurs qui permettent de guider le tribunal au moment de déterminer si l'ordonnance constitue une réclamation prouvable, notamment si les activités se poursuivent, si le débiteur exerce un contrôle sur le bien et s'il dispose des moyens de se conformer à l'ordonnance. Il est également possible pour le tribunal de prendre en compte les conséquences qu'entraînerait sur le processus d'insolvabilité le fait d'exiger du débiteur qu'il se conforme à l'ordonnance. Puisque l'analyse qu'il convient de réaliser est fondée sur les faits propres à chaque cas, il n'est pas nécessaire que tous ces indicateurs soient présents, et d'autres peuvent également devenir pertinents.

[39] Après avoir souligné les trois conditions qui permettent en l'espèce de conclure qu'une ordonnance constitue une réclamation prouvable dans le cadre d'un processus régi par la *LACC*, il me faut examiner certains arguments de principe que la province et certains intervenants ont fait valoir.

[40] Ils ont plaidé que le fait d'assimiler une ordonnance d'un organisme administratif à une réclamation dans le cadre de procédure en insolvabilité éteint les obligations environnementales auxquelles le débiteur est tenu, minant par le fait même le principe du pollueur-payeur examiné par notre Cour dans l'arrêt *Cie pétrolière Impériale*

demonstrates a misunderstanding of the nature of insolvency proceedings. Subjecting an order to the claims process does not extinguish the debtor's environmental obligations any more than subjecting any creditor's claim to that process extinguishes the debtor's obligation to pay its debts. It merely ensures that the creditor's claim will be paid in accordance with insolvency legislation. Moreover, full compliance with orders that are found to be monetary in nature would shift the costs of remediation to third-party creditors, including involuntary creditors, such as those whose claims lie in tort or in the law of extra-contractual liability. In the insolvency context, the Province's position would result not only in a super-priority, but in the acceptance of a "third-party-pay" principle in place of the polluter-pay principle.

[41] Nor does subjecting the orders to the insolvency process amount to issuing a licence to pollute, since insolvency proceedings do not concern the debtor's future conduct. A debtor that is reorganized must comply with all environmental regulations going forward in the same way as any other person. To quote the colourful analogy of two American scholars, "Debtors in bankruptcy have — and should have — no greater license to pollute in violation of a statute than they have to sell cocaine in violation of a statute" (D. G. Baird and T. H. Jackson, "Comment: *Kovacs* and Toxic Wastes in Bankruptcy" (1984), 36 *Stan. L. Rev.* 1199, at p. 1200).

[42] Furthermore, corporations may engage in activities that carry risks. No matter what risks are at issue, reorganization made necessary by insolvency is hardly ever a deliberate choice. When the risks materialize, the dire costs are borne by almost all stakeholders. To subject orders to the claims process is not to invite corporations to restructure

ltée c. Québec (Ministre de l'Environnement), 2003 CSC 58, [2003] 2 R.C.S. 624, par. 24. Cet argument démontre une mauvaise compréhension de la nature des procédures en matière d'insolvabilité. Le fait d'assujettir une ordonnance au processus de réclamations n'éteint pas les obligations environnementales qui incombent au débiteur, pas plus que le fait de soumettre à ce processus les réclamations des créanciers n'éteint l'obligation du débiteur de payer ses dettes. Le fait d'assujettir une ordonnance au processus de réclamation vise simplement à faire en sorte que le paiement au créancier sera fait conformément aux dispositions législatives applicables en matière d'insolvabilité. De plus, le respect intégral des ordonnances dont la nature pécuniaire est reconnue transférerait le coût de la décontamination aux tiers créanciers, y compris aux créanciers involontaires, par exemple les créanciers en responsabilité délictuelle ou extra-contractuelle. Dans un contexte d'insolvabilité, la position de la province aurait comme résultat de lui accorder non seulement une super-priorité, mais aussi de reconnaître l'application d'un principe du « tiers-payeur » plutôt que celui du pollueur-payeur.

[41] Par ailleurs, l'assujettissement des ordonnances au processus d'insolvabilité n'autorise pas une personne à polluer, car la procédure en insolvabilité ne touche pas les actes que le débiteur posera dans le futur. Le débiteur réorganisé doit se conformer pour l'avenir à la réglementation environnementale, comme le ferait toute autre personne. Pour citer une analogie haute en couleurs de deux universitaires américains, [TRADUCTION] « [l]es débiteurs en faillite n'ont pas — et ne devraient pas avoir — une autorisation plus étendue de polluer en violation d'une loi qu'ils n'en ont de vendre de la cocaïne » (D. G. Baird et T. H. Jackson, « Comment : *Kovacs* and Toxic Wastes in Bankruptcy » (1984), 36 *Stan. L. Rev.* 1199, p. 1200).

[42] En outre, il arrive que des sociétés exercent des activités comportant des risques. Peu importe les risques en cause, une réorganisation rendue nécessaire par l'insolvabilité de la société peut difficilement être assimilée à un choix délibéré. Lorsque les risques se concrétisent, la quasi-totalité des personnes ayant des intérêts dans la société en

in order to rid themselves of their environmental liabilities.

[43] And the power to determine whether an order is a provable claim does not mean that the court will necessarily conclude that the order before it will be subject to the *CCAA* process. In fact, the *CCAA* court in the case at bar recognized that orders relating to the environment may or may not be considered provable claims. It stayed only those orders that were monetary in nature.

[44] The Province also argues that courts have in the past held that environmental orders cannot be interpreted as claims when the regulatory body has not yet exercised its power to assert a claim framed in monetary terms. The Province relies in particular on *Panamericana de Bienes y Servicios S.A. v. Northern Badger Oil & Gas Ltd.* (1991), 81 Alta. L.R. (2d) 45 (C.A.), and its progeny. In *Panamericana*, the Alberta Court of Appeal held that a receiver was personally liable for work under a remediation order and that the order was not a claim in insolvency proceedings. The court found that the duty to undertake remediation work is owed to the public at large until the regulator exercises its power to assert a monetary claim.

[45] The first answer to the Province's argument is that courts have never shied away from putting substance ahead of form. They can determine whether the order is in substance monetary.

[46] The second answer is that the provisions relating to the assessment of claims, particularly those governing contingent claims, contemplate instances in which the quantum is not yet established when the claims are filed. Whether, in the

supportent les terribles coûts. L'assujettissement des ordonnances à la procédure de réclamations n'équivaut pas à convier les sociétés à se réorganiser dans le but d'échapper à leurs obligations environnementales.

[43] Et le pouvoir de déterminer si une ordonnance constitue une réclamation prouvable ne signifie pas que le tribunal jugera nécessairement que l'ordonnance sera soumise au processus de réorganisation. En fait, le tribunal en l'espèce a reconnu que les ordonnances environnementales pouvaient être ou ne pas être considérées comme des réclamations prouvables. Il n'a rendu une ordonnance de suspension qu'à l'égard des ordonnances de nature pécuniaire.

[44] La province plaide aussi que selon la jurisprudence, les ordonnances environnementales ne peuvent pas être assimilées à des réclamations lorsque l'organisme administratif n'a pas encore exercé son pouvoir de faire valoir une réclamation formulée en termes pécuniaires. La province s'appuie particulièrement sur l'arrêt *Panamericana de Bienes y Servicios S.A. c. Northern Badger Oil & Gas Ltd.* (1991), 81 Alta. L.R. (2d) 45 (C.A.), et les jugements rendus dans sa foulée. Dans l'arrêt *Panamericana*, la Cour d'appel de l'Alberta a tenu le séquestre personnellement responsable de l'exécution des travaux ordonnés et a statué que l'ordonnance ne constituait pas une réclamation visée par les procédures en insolvabilité. La cour a conclu que l'obligation d'entreprendre les travaux de décontamination est due au public en général jusqu'à ce que l'organisme administratif exerce son pouvoir de faire valoir une réclamation pécuniaire.

[45] La première réponse à cet argument de la province est que les tribunaux n'ont jamais hésité à privilégier le fond à la forme. Les tribunaux peuvent déterminer si, en substance, l'ordonnance est de nature pécuniaire.

[46] La seconde réponse est que les dispositions concernant l'évaluation des réclamations, en particulier celles régissant les réclamations éventuelles, n'exigent pas que la valeur pécuniaire soit établie au moment où elles sont produites. Un

regulatory context, an obligation always entails the existence of a correlative right has been discussed by a number of scholars. Various theories of rights have been put forward (see W. N. Hohfeld, *Fundamental Legal Conceptions as Applied in Judicial Reasoning* (new ed. 2001); D. N. MacCormick, "Rights in Legislation", in P. M. S. Hacker and J. Raz, eds., *Law, Morality, and Society: Essays in Honour of H. L. A. Hart* (1977), 189). However, because the Province issued the orders in this case, it would be recognized as a creditor in respect of a right no matter which of these theories was applied. As interesting as the discussion may be, therefore, I do not need to consider which theory should prevail. The real question is not to whom the obligation is owed, as this question is answered by the statute, which determines who can require that it be discharged. Rather, the question is whether it is sufficiently certain that the regulatory body will perform the remediation work and, as a result, have a monetary claim.

[47] The third answer to the Province's argument is that insolvency legislation has evolved considerably over the two decades since *Panamericana*. At the time of *Panamericana*, none of the provisions relating to environmental liabilities were in force. Indeed, some of those provisions were enacted very soon after, and seemingly in response to, that case. In 1992, Parliament shielded trustees from the very liability imposed on the receiver in *Panamericana* (*An Act to amend the Bankruptcy Act and to amend the Income Tax Act in consequence thereof*, S.C. 1992, c. 27, s. 9, amending s. 14 of the *BIA*). The 1997 amendments provided additional protection to trustees and monitors (*An Act to amend the Bankruptcy and Insolvency Act, the Companies' Creditors Arrangement Act and the Income Tax Act*, S.C. 1997, c. 12). The 2007 amendments made it clear that a *CCAA* court has the power to determine that a regulatory order may be a claim and also provided criteria for staying regulatory orders (s. 65, amending the *CCAA* to include the current version of s. 11.1). The purpose of these amendments was to balance the creditor's

certain nombre d'auteurs ont examiné la question de savoir si, dans un contexte réglementaire, l'existence d'une obligation implique toujours en corrélation celle d'un droit. Diverses théories relatives aux droits ont été avancées (voir W. N. Hohfeld, *Fundamental Legal Conceptions as Applied in Judicial Reasoning* (nouvelle éd. 2001); D. N. MacCormick, « Rights in Legislation », dans P. M. S. Hacker et J. Raz, dir., *Law, Morality, and Society : Essays in Honour of H. L. A. Hart* (1977), 189). Toutefois, comme en l'espèce la province a prononcé les ordonnances, elle serait reconnue comme créancière d'un droit en vertu de l'une ou l'autre de ces théories. Par conséquent, malgré l'intérêt que peut susciter ce débat, il n'est pas nécessaire de déterminer la théorie qui prévaut. La véritable question n'est pas de savoir à qui est due l'obligation, puisque la loi y répond en indiquant qui peut en exiger l'exécution. La question est plutôt de savoir s'il est suffisamment certain que l'organisme administratif effectuera les travaux de décontamination et pourra ainsi faire valoir une réclamation pécuniaire.

[47] La troisième réponse à l'argument soulevé par la province est que la législation en matière d'insolvabilité a considérablement évolué au cours des deux décennies écoulées depuis l'arrêt *Panamericana*. À l'époque où l'arrêt *Panamericana* a été prononcé, aucune des dispositions concernant les obligations liées à l'environnement n'était en vigueur. Certaines des dispositions ont été adoptées très peu de temps après cette décision et, semble-t-il, en réponse à celle-ci. En 1992, le législateur a permis aux syndics d'échapper à la responsabilité même que l'arrêt *Panamericana* avait retenue contre le séquestre (*Loi modifiant la Loi sur la faillite et la Loi de l'impôt sur le revenu en conséquence*, L.C. 1992, ch. 27, art. 9, modifiant l'art. 14 de la *LFI*). Une protection additionnelle a été accordée au syndic et au contrôleur avec les modifications adoptées en 1997 (*Loi modifiant la Loi sur la faillite et l'insolvabilité, la Loi sur les arrangements avec les créanciers des compagnies et la Loi de l'impôt sur le revenu*, L.C. 1997, ch. 12). Les modifications apportées en 2007 ont précisé que le tribunal chargé d'appliquer la *LACC* a

need for fairness against the debtor's need to make a fresh start.

[48] Whether the regulatory body has a contingent claim is a determination that must be grounded in the facts of each case. Generally, a regulatory body has discretion under environmental legislation to decide how best to ensure that regulatory obligations are met. Although the court should take care to avoid interfering with that discretion, the action of a regulatory body is nevertheless subject to scrutiny in insolvency proceedings.

V. Application

[49] I now turn to the application of the principles discussed above to the case at bar. This case does not turn on whether the Province is the creditor of an obligation or whether damage had occurred as of the relevant date. Those requirements are easily satisfied, since the Province had identified itself as a creditor by resorting to *EPA* enforcement mechanisms and since the damage had occurred before the time of the *CCAA* proceedings. Rather, the issue centres on the third requirement: that the orders meet the criterion for admission as a pecuniary claim. The claim was contingent to the extent that the Province had not yet formally exercised its power to ask for the payment of money. The question is whether it was sufficiently certain that the orders would eventually result in a monetary claim. To the *CCAA* judge, there was no doubt that the answer was yes.

le pouvoir de décider qu'une ordonnance d'un organisme administratif peut constituer une réclamation; ces modifications ont de plus établi des critères applicables à la suspension de ces ordonnances (art. 65, modifiant la *LACC* par l'ajout de l'art. 11.1). Ces modifications visaient à établir un équilibre entre le besoin de traiter les créanciers de façon équitable et celui de permettre au débiteur de prendre un nouveau départ.

[48] La détermination qu'une ordonnance d'un organisme administratif constitue une réclamation éventuelle doit être fondée sur les faits de chaque affaire. La législation en matière d'environnement accorde généralement à un organisme administratif un pouvoir discrétionnaire de décider de la meilleure façon d'assurer le respect des obligations découlant de la réglementation. Quoique le tribunal doive se garder de s'ingérer dans l'exercice du pouvoir discrétionnaire de ces organismes, les mesures qu'ils prennent peuvent néanmoins faire l'objet d'un examen dans le cadre de procédures engagées sous le régime fédéral de l'insolvabilité.

V. Application

[49] J'aborde maintenant l'application des principes énoncés ci-dessus à l'affaire dont notre Cour est saisie. En l'espèce, le débat n'est pas centré sur la question de savoir si la province est créancière d'une obligation ou si des dommages étaient survenus à la date pertinente. Il est facile de répondre à ces questions étant donné que la province s'est elle-même présentée comme créancière en ayant recours aux mécanismes d'application de l'*EPA* et que les dommages sont survenus avant que les procédures en vertu de la *LACC* ne soient entamées. Le débat porte plutôt sur la troisième condition, celle qui consiste à savoir si les ordonnances satisfont au critère d'admissibilité à titre de réclamation pécuniaire. La réclamation était éventuelle dans la mesure où la province n'avait pas formellement exercé son pouvoir de demander paiement d'une somme d'argent. La question est de savoir s'il était suffisamment certain que l'ordonnance mènerait éventuellement à la production d'une réclamation pécuniaire. Pour le juge de première instance, une réponse affirmative ne faisait pas de doute.

[50] The Province's exercise of its legislative powers in enacting the *Abitibi Act* created a unique set of facts that led to the orders being issued. The seizure of Abitibi's assets by the Province, the cancellation of all outstanding water and hydroelectric contracts between Abitibi and the Province, the cancellation of pending legal proceedings by Abitibi in which it sought the reimbursement of several hundreds of thousands of dollars, and the denial of any compensation for the seized assets and of legal redress are inescapable background facts in the judge's review of the *EPA* Orders.

[51] The *CCAA* judge did not elaborate on whether it was sufficiently certain that the Minister would perform the remediation work and therefore make a monetary claim. However, most of his findings clearly rest on a positive answer to this question. For example, his finding that "[i]n all likelihood, the pith and substance of the EPA Orders is an attempt by the Province to lay the groundwork for monetary claims against Abitibi, to be used most probably as an offset in connection with Abitibi's own NAFTA claims for compensation" (para. 178), is necessarily based on the premise that the Province would most likely perform the remediation work. Indeed, since monetary claims must, both at common law and in civil law, be mutual for set-off or compensation to operate, the Province had to have incurred costs in doing the work in order to have a claim that could be set off against Abitibi's claims.

[52] That the judge relied on an implicit finding that the Province would most likely perform the work and make a claim to offset its costs is also shown by the confirmation he found in the declaration by the Premier that the Province was attempting to assess the cost of doing remediation work Abitibi had allegedly left undone and that in the Province's assessment, "at this point in

[50] En adoptant l'*Abitibi Act*, ayant ainsi recours à son pouvoir législatif, la province mettait en place un contexte factuel unique qui menait à l'émission des ordonnances. La saisie par la province des actifs d'Abitibi, l'annulation de tous les contrats d'approvisionnement en eau et d'hydroélectricité conclus entre Abitibi et la province, l'annulation des recours intentés par Abitibi pour obtenir le remboursement de plusieurs centaines de milliers de dollars et le refus de toute indemnité et de tous recours en justice à l'égard des actifs saisis tissent un contexte factuel dont le juge ne peut faire abstraction dans son examen des ordonnances *EPA*.

[51] Le juge de première instance n'a pas fait une analyse distincte du critère suivant lequel le tribunal doit être suffisamment certain que le ministre exécuterait les travaux de décontamination et ferait, par conséquent, valoir une réclamation pécuniaire. Cependant, la plupart de ses conclusions reposent manifestement sur un constat positif à cet égard. Par exemple, le constat que [TRADUCTION] « [s]elon toute vraisemblance, le caractère véritable des ordonnances *EPA* [consiste] pour la province à tenter de jeter les bases de réclamations pécuniaires contre Abitibi, dans le but de les utiliser tout probablement à titre compensatoire au regard des demandes d'indemnisation d'Abitibi fondées sur l'ALÉNA » (par. 178) repose nécessairement sur la prémisse que la province allait fort probablement exécuter les travaux de décontamination. En effet, puisque les réclamations pécuniaires, en common law comme en droit civil, doivent être réciproques pour opérer compensation, la province devait avoir engagé des dépenses en exécutant des travaux, ce qui établissait la base de la réclamation qu'elle ferait valoir pour compenser celle d'Abitibi.

[52] Un autre fait illustre que le juge de première instance a implicitement conclu que la province allait fort probablement exécuter les travaux et produire une réclamation pour compenser ses coûts est qu'il en a trouvé une confirmation dans la déclaration du premier ministre selon laquelle la province tentait d'évaluer ce qu'il en coûterait pour réaliser les travaux de décontamination qu'Abitibi n'aurait

time, there would not be a net payment to Abitibi" (para. 181).

[53] The *CCAA* judge's reasons not only rest on an implicit finding that the Province would most likely perform the work, but refer explicitly to facts that support this finding. To reach his conclusion that the *EPA* Orders were monetary in nature, the *CCAA* judge relied on the fact that Abitibi's operations were funded through debtor-in-possession financing and its access to funds was limited to ongoing operations. Given that the *EPA* Orders targeted sites that were, for the most part, no longer in Abitibi's possession, this meant that Abitibi had no means to perform the remediation work during the reorganization process.

[54] In addition, because Abitibi lacked funds and no longer controlled the properties, the timetable set by the Province in the *EPA* Orders suggested that the Province never truly intended that Abitibi was to perform the remediation work required by the orders. The timetable was also unrealistic. For example, the orders were issued on November 12, 2009 and set a deadline of January 15, 2010 to perform a particular act, but the evidence revealed that compliance with this requirement would have taken close to a year.

[55] Furthermore, the judge relied on the fact that Abitibi was not simply designated a "person responsible" under the *EPA*, but was intentionally targeted by the Province. The finding that the Province had targeted Abitibi was drawn not only from the timing of the *EPA* Orders, but also from the fact that Abitibi was the only person designated in them, whereas others also appeared to be responsible — in some cases, primarily responsible — for the contamination. For example, Abitibi was ordered to do remediation work on a site it had surrendered more than 50 years before the orders were issued; the expert report upon which the orders were based made no distinction between Abitibi's activities on the property, on which its source of power had been horse power, and subsequent activities by others who had used fuel-powered vehicles

pas exécutés, et que selon l'estimation de la province, [TRADUCTION] « à l'heure actuelle, aucun paiement net ne serait versé à Abitibi » (par. 181).

[53] Les motifs du juge de première instance reposent non seulement sur une constatation implicite que la province exécuterait fort probablement les travaux, mais ils renvoient expressément aux faits qui appuient cette constatation. Pour conclure que les ordonnances *EPA* étaient de nature pécuniaire, le juge s'est fondé sur le fait qu'Abitibi pouvait mener ses opérations grâce à un financement de débiteur-exploitant et qu'elle n'avait accès à ces fonds que pour ses activités courantes. Étant donné que les ordonnances visaient des sites que, pour la plupart, Abitibi ne possédait plus, cela signifiait qu'Abitibi ne disposait d'aucune ressource pour exécuter les travaux pendant la réorganisation.

[54] De plus, parce qu'Abitibi ne disposait pas des fonds et n'exerçait plus aucun contrôle sur les biens, l'échéancier fixé par la province dans les ordonnances *EPA* était non seulement irréaliste, mais suggérait que la province n'avait jamais vraiment eu l'intention qu'Abitibi exécute les travaux qu'elle lui ordonnait de faire. Par exemple, les ordonnances en date du 12 novembre 2009 exigeaient que certains travaux particuliers soient terminés le 15 janvier 2010 alors que la preuve démontre qu'il aurait fallu presque un an pour exécuter ces travaux.

[55] En outre, le juge s'est appuyé sur le fait qu'Abitibi n'était pas simplement désignée comme [TRADUCTION] « personne responsable » aux termes de l'*EPA*, mais qu'elle était intentionnellement visée par la province. Il a fait cette constatation non seulement en raison du choix du moment où les ordonnances ont été prononcées, mais aussi parce qu'Abitibi y était la seule personne désignée alors que d'autres semblaient également responsables — et en certains cas, principalement responsables — de la contamination. Par exemple, la province a ordonné à Abitibi d'effectuer des travaux de décontamination d'un site qu'elle avait abandonné plus de 50 ans avant le prononcé des ordonnances alors que le rapport d'expert sur lequel les ordonnances étaient fondées ne distinguait aucunement les activités d'Abitibi, qui avait utilisé des chevaux,

there. In the judge's opinion, this finding of fact went to the Province's intent to establish a basis for performing the work itself and asserting a claim against Abitibi.

[56] These reasons — and others — led the *CCAA* judge to conclude that the Province had not expected Abitibi to perform the remediation work and that the "intended, practical and realistic effect of the EPA Orders was to establish a basis for the Province to recover amounts of money to be eventually used for the remediation of the properties in question" (para. 211). He found that the Province appeared to have in fact taken some steps to liquidate the claims arising out of the *EPA* Orders.

[57] In the end, the judge found that there was definitely a claim that "might" be filed, and that it was not left to "the subjective choice of the creditor to hold the claim in its pocket for tactical reasons" (para. 227). In his words, the situation did not involve a "detached regulator or public enforcer issuing [an] order for the public good" (para. 175), and it was "the hat of a creditor that best fi[t] the Province, not that of a disinterested regulator" (para. 176).

[58] In sum, although the analytical framework used by Gascon J. was driven by the facts of the case, he reviewed all the legal principles and facts that needed to be considered in order to make the determination in the case at bar. He did at times rely on indicators that are unique and that do not appear in the analytical framework I propose above, but he did so because of the exceptional facts of this case. Yet, had he formulated the question in the same way as I have, his conclusion, based on his objective findings of fact, would have been the same. Earmarking money may be a strong indicator that a province will perform remediation work, and actually commencing the work is the first step towards the creation of a debt, but these are not the

et les activités subséquentes d'autres personnes qui y avaient utilisé des véhicules alimentés au mazout. Ce fait, pour le juge, illustrait l'intention de la province d'établir un fondement pour exécuter elle-même les travaux et présenter une réclamation contre Abitibi.

[56] Ces motifs — et d'autres — ont amené le juge de première instance à conclure que la province ne s'attendait pas à ce qu'Abitibi exécute les travaux de décontamination et que [TRADUCTION] « les ordonnances *EPA* avaient pour effet voulu, pratique et réaliste de jeter les bases qui permettraient à la province de recouvrer les sommes d'argent devant éventuellement être employées pour la décontamination des terrains en question » (par. 211). Il a conclu que la province semblait avoir en fait pris des mesures en vue de liquider les réclamations découlant des ordonnances *EPA*.

[57] En fin de compte, le juge a conclu qu'il existait véritablement une réclamation qui « pourrait » être présentée, et qu'on ne pouvait laisser au bon vouloir du créancier [TRADUCTION] « le choix subjectif de la garder en réserve pour des raisons tactiques » (par. 227). Pour reprendre ses propres mots, il ne s'agissait pas d'un cas où « un organisme de réglementation ou d'application de la loi a émis de manière objective une ordonnance dans l'intérêt public » (par. 175), mais que « la province a agi plus comme un créancier que comme un organisme administratif désintéressé » (par. 176).

[58] En somme, bien que le cadre analytique utilisé par le juge Gascon a été dicté par les faits de l'affaire, il a examiné tous les principes juridiques et les faits qu'il était tenu de prendre en compte pour statuer sur la question qui se posait. À l'occasion, il s'est appuyé sur des indicateurs singuliers qui ne figurent pas dans le cadre analytique que j'ai déjà proposé, mais cela s'explique par les faits exceptionnels en l'espèce. Or, s'il avait formulé la question comme je l'ai posée, sa conclusion, appuyée sur ses constatations de fait objectives, aurait été la même. Le fait de prévoir un budget peut constituer un indicateur clair qu'une province exécutera des travaux de décontamination, et le fait que ces travaux soient entrepris constitue la première étape de

only considerations that can lead to a finding that a creditor has a monetary claim. The *CCAA* judge's assessment of the facts, particularly his finding that the *EPA* Orders were the first step towards performance of the remediation work by the Province, leads to no conclusion other than that it was sufficiently certain that the Province would perform remediation work and therefore fall within the definition of a creditor with a monetary claim.

la constitution d'une dette, mais ces considérations ne sont pas les seules qui permettent de conclure qu'un créancier fait valoir une réclamation pécuniaire. L'appréciation des faits par le juge de première instance, plus particulièrement sa constatation que les ordonnances constituaient la première étape en vue de la décontamination des sites, ne permet de tirer aucune conclusion autre que celle suivant laquelle il était suffisamment certain que la province exécuterait des travaux de décontamination et qu'elle était par conséquent visée par la définition d'un créancier ayant une réclamation pécuniaire.

VI. Conclusion

VI. Conclusion

[59] In sum, I agree with the Chief Justice that, as a general proposition, an environmental order issued by a regulatory body can be treated as a contingent claim, and that such a claim can be included in the claims process if it is sufficiently certain that the regulatory body will make a monetary claim against the debtor. Our difference of views lies mainly in the applicable threshold for including contingent claims and in our understanding of the *CCAA* judge's findings of fact.

[59] En somme, je suis d'accord avec la Juge en chef pour dire qu'en règle générale, une ordonnance environnementale d'un organisme administratif peut être traitée comme une réclamation éventuelle et qu'une telle réclamation peut être incluse au processus de réclamation s'il est suffisamment certain que l'organisme administratif fera valoir une réclamation pécuniaire contre le débiteur. Nos divergences de vues portent principalement sur le critère applicable pour que les réclamations éventuelles soient incluses et sur la façon dont nous interprétons les constatations de fait tirées par le juge de première instance.

[60] With respect to the law, the Chief Justice would craft a standard specific to the context of environmental orders by requiring a "likelihood approaching certainty" that the regulatory body will perform the remediation work. She finds that this threshold is justified because "remediation may cost a great deal of money" (para. 86). I acknowledge that remediating pollution is often costly, but I am of the view that Parliament has borne this consideration in mind in enacting provisions specific to environmental claims. Moreover, I recall that in this case, the Premier announced that the remediation work would be performed at no net cost to the Province. It was clear to him that the *Abitibi Act* would make it possible to offset all the related costs.

[60] En ce qui concerne le droit, la Juge en chef établirait une norme propre au contexte des ordonnances environnementales qui exigerait une « probabilité proche de la certitude » que l'organisme administratif réalisera les travaux de restauration. Elle estime que ce critère s'impose parce que « les travaux de restauration peuvent être très coûteux » (par. 86). Je reconnais que les travaux de décontamination sont souvent coûteux, mais je crois que cette considération a été prise en compte par le législateur fédéral lors de l'adoption des dispositions particulières visant les réclamations en matière environnementale. De plus, je rappelle qu'en l'instance, le premier ministre a annoncé que les travaux de décontamination seraient réalisés sans coût net pour la province. Il était évident pour lui que l'adoption de l'*Abitibi Act* permettrait de compenser tous les coûts afférents.

[61] Thus, I prefer to take the approach generally taken for all contingent claims. In my view, the *CCAA* court is entitled to take all relevant facts into consideration in making the relevant determination. Under this approach, the contingency to be assessed in a case such as this is whether it is sufficiently certain that the regulatory body will perform remediation work and be in a position to assert a monetary claim.

[62] Finally, the Chief Justice would review the *CCAA* court's findings of fact. I would instead defer to them. On those findings, applying any legal standard, be it the one proposed by the Chief Justice or the one I propose, the Province's claim is monetary in nature and its motion for a declaration exempting the *EPA* Orders from the claims procedure order was properly dismissed.

[63] For these reasons, I would dismiss the appeal with costs.

The following are the reasons delivered by

THE CHIEF JUSTICE (dissenting) —

1. Overview

[64] The issue in this case is whether orders made under the *Environmental Protection Act*, S.N.L. 2002, c. E-14.2 ("*EPA*"), by the Newfoundland and Labrador Minister of Environment and Conservation ("Minister") requiring a polluter to clean up sites (the "*EPA* Orders") are monetary claims that can be compromised in corporate restructuring under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). If they are not claims that can be compromised in restructuring, the Abitibi respondents ("Abitibi") will still have a legal obligation to clean up the sites following their emergence from restructuring. If they are such claims, Abitibi will have emerged from restructuring free of the obligation, able to recommence business without remediating the

[61] Par conséquent, je préfère retenir la méthode généralement suivie en matière de réclamations éventuelles. À mon avis, le tribunal chargé de l'application de la *LACC* peut prendre en compte l'ensemble des faits pertinents en vue de rendre la décision appropriée. Suivant cette approche, l'éventualité qu'il faut évaluer dans une affaire comme celle-ci est de savoir s'il est suffisamment certain que l'organisme administratif exécutera les travaux de décontamination et sera en mesure de faire valoir une réclamation pécuniaire.

[62] Enfin, la Juge en chef réviserait les conclusions de fait du juge de première instance. Pour ma part, je m'en remets à ces conclusions. Quelle que soit la norme juridique appliquée, soit celle proposée par la Juge en chef ou celle que je propose, au vu de ces conclusions, la réclamation de la province est de nature pécuniaire et sa requête demandant de déclarer que les ordonnances *EPA* n'étaient pas assujetties à l'ordonnance relative à la procédure de réclamations a été à juste titre rejetée.

[63] Pour ces motifs, je suis d'avis de rejeter le pourvoi avec dépens

Version française des motifs rendus par

LA JUGE EN CHEF (dissidente) —

1. Aperçu

[64] Il s'agit en l'espèce de savoir si des ordonnances du ministre de l'Environnement et de la Conservation (le « ministre ») de Terre-Neuve-et-Labrador, émises en vertu de l'*Environmental Protection Act*, S.N.L. 2002, ch. E-14.2 (« *EPA* »), obligeant un pollueur à décontaminer des sites (les « ordonnances *EPA* ») constituent des réclamations pécuniaires qui peuvent faire l'objet d'une transaction dans le cadre d'une restructuration d'entreprise engagée sous le régime de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, ch. C-36 (« *LACC* »). Si elles ne constituent pas des réclamations pécuniaires pouvant faire l'objet d'une transaction, les intimées du groupe Abitibi (« Abitibi ») auront encore l'obligation légale de décontaminer les sites lorsque leur

properties it polluted, the cost of which will fall on the Newfoundland and Labrador public.

restructuration sera terminée. Dans le cas contraire, Abitibi sera dégagée de cette obligation; elle pourra reprendre ses activités à l'issue de la restructuration sans avoir à décontaminer les sites qu'elle a pollués et la population de Terre-Neuve-et-Labrador devra supporter le coût de la décontamination.

[65] Remediation orders made under a province's environmental protection legislation impose ongoing regulatory obligations on the corporation required to clean up the pollution. They are not monetary claims. In narrow circumstances, specified by the *CCAA*, these ongoing regulatory obligations may be reduced to monetary claims, which can be compromised under *CCAA* proceedings. This occurs where a province has done the work, or where it is "sufficiently certain" that it will do the work. In these circumstances, the regulatory obligation would be extinguished and the province would have a monetary claim for the cost of remediation in the *CCAA* proceedings. Otherwise, the regulatory obligation survives the restructuring.

[65] Les ordonnances exigeant la décontamination émises aux termes d'une loi provinciale sur la protection de l'environnement imposent des exigences réglementaires continues à la personne morale requise de remédier à la pollution. Ces ordonnances ne constituent pas des réclamations pécuniaires. En certaines circonstances particulières prévues par la *LACC*, ces exigences réglementaires continues peuvent être converties en réclamations pécuniaires, lesquelles peuvent faire l'objet de transactions dans le cadre de procédures engagées aux termes de la *LACC*. Cette situation se produit lorsqu'une province a exécuté les travaux, ou lorsqu'il est « suffisamment certain » qu'elle exécutera les travaux. Dans ces circonstances, l'exigence réglementaire serait éteinte et la province pourrait produire, dans le cadre de procédures engagées sous le régime de la *LACC*, une réclamation pécuniaire couvrant le coût des travaux de décontamination. Autrement, l'exigence réglementaire subsiste après la restructuration.

[66] In my view, the orders for remediation in this case, with a minor exception, are not claims that can be compromised in restructuring. On one of the properties, the Minister did emergency remedial work and put other work out to tender. These costs can be claimed in the *CCAA* proceedings. However, with respect to the other properties, on the evidence before us, the Minister has neither done the clean-up work, nor is it sufficiently certain that he or she will do so. The Province of Newfoundland and Labrador ("Province") retained a number of options, including requiring Abitibi to perform the remediation if it successfully emerged from the *CCAA* restructuring.

[66] À mon avis, les ordonnances exigeant la décontamination en l'espèce, à une exception près, ne constituent pas des réclamations pouvant faire l'objet de transactions dans le cadre d'une restructuration. Dans un des sites, la ministre de l'époque a effectué d'urgence la décontamination et a lancé un appel d'offres pour d'autres travaux. Le coût de ces travaux peut faire l'objet d'une réclamation dans les procédures engagées sous le régime de la *LACC*. Toutefois, en ce qui concerne les autres sites, selon les éléments de preuve dont nous disposons, le ministre en poste n'a pas effectué les travaux de décontamination et il n'est pas suffisamment certain qu'il le fera. La province de Terre-Neuve-et-Labrador (« province ») a conservé un certain nombre de solutions, dont celle d'obliger Abitibi à décontaminer les sites si elle réussit sa restructuration engagée sous le régime de la *LACC*.

[67] I would therefore allow the appeal and grant the Province the declaration it seeks that Abitibi is still subject to its obligations under the *EPA* following its emergence from restructuring, except for work done or tendered for on the Buchans site.

2. The Proceedings Below

[68] The *CCAA* judge took the view that the Province issued the *EPA* Orders, not in order to make Abitibi remediate, but as part of a money grab. He therefore concluded that the orders were monetary and financial in nature and should be considered claims that could be compromised under the *CCAA* (2010 QCCS 1261, 68 C.B.R. (5th) 1). The Quebec Court of Appeal denied leave to appeal on the ground that this "factual" conclusion could not be disturbed (2010 QCCA 965, 68 C.B.R. (5th) 57).

[69] The *CCAA* judge's stark view that an *EPA* obligation can be considered a monetary claim capable of being compromised simply because (as he saw it) the Province's motive was money, is no longer pressed. Whether an *EPA* order is a claim under the *CCAA* depends on whether it meets the requirements for a claim under that statute. That is the only issue to be resolved. Insofar as this determination touches on the division of powers, I am in substantial agreement with my colleague Deschamps J., at paras. 18-19.

3. The Distinction Between Regulatory Obligations and Claims Under the *CCAA*

[70] Orders to clean up polluted property under provincial environmental protection legislation are regulatory orders. They remain in effect until the

[67] Je suis par conséquent d'avis d'accueillir le pourvoi et d'accorder à la province le jugement déclaratoire sollicité portant qu'Abitibi reste assujettie à ses obligations en vertu de l'*EPA* au terme de cette période de restructuration, à l'exception des travaux sur le site de Buchans déjà exécutés ou à l'égard desquels des appels d'offres ont été lancés.

2. Les décisions des juridictions inférieures

[68] Le juge de première instance a adopté le point de vue selon lequel la province avait émis les ordonnances *EPA*, non pas pour obliger Abitibi à réparer les dommages causés, mais pour lui soutirer de l'argent. Il a donc conclu que les ordonnances étaient de nature pécuniaire et financière, et qu'elles devraient être considérées comme des réclamations pouvant faire l'objet de transactions sous le régime de la *LACC* (2010 QCCS 1261, 68 C.B.R. (5th) 1). La Cour d'appel du Québec a refusé l'autorisation d'interjeter appel de cette décision au motif que rien ne permettait de modifier cette conclusion « de fait » (2010 QCCA 965, 68 C.B.R. (5th) 57).

[69] Le point de vue peu nuancé du juge de première instance, selon lequel une obligation découlant de l'*EPA* peut être considérée comme une réclamation pécuniaire susceptible de faire l'objet d'une transaction du simple fait (à son avis) que la province n'était motivée que par l'argent, n'est plus en cause. Pour répondre à la question de savoir si une ordonnance émise sous le régime de l'*EPA* constitue une réclamation au sens de la *LACC*, il faut déterminer si elle satisfait aux conditions d'existence d'une réclamation établies par cette loi. Il s'agit de la seule question à trancher. Dans la mesure où la décision sur ce point touche le partage des pouvoirs, je souscris pour l'essentiel à l'opinion exprimée par ma collègue la juge Deschamps aux par. 18-19.

3. La distinction entre une exigence réglementaire et une réclamation au titre de la *LACC*

[70] Les ordonnances exigeant la décontamination des sites pollués émises en vertu des lois provinciales sur l'environnement sont des ordonnances

property has been cleaned up or the matter otherwise resolved.

[71] It is not unusual for corporations seeking to restructure under the *CCAA* to be subject to a variety of ongoing regulatory orders arising from statutory schemes governing matters like employment, energy conservation and the environment. The corporation remains subject to these obligations as it continues to carry on business during the restructuring period, and remains subject to them when it emerges from restructuring unless they have been compromised or liquidated.

[72] The *CCAA*, like the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"), draws a fundamental distinction between ongoing regulatory obligations owed to the public, which generally survive the restructuring, and monetary claims that can be compromised.

[73] This distinction is also recognized in the jurisprudence, which has held that regulatory duties owed to the public are not "claims" under the *BIA*, nor, by extension, under the *CCAA*. In *Panamericana de Bienes y Servicios S.A. v. Northern Badger Oil & Gas Ltd.* (1991), 81 Alta. L.R. (2d) 45, the Alberta Court of Appeal held that a receiver in bankruptcy must comply with an order from the Energy Resources Conservation Board to comply with well abandonment requirements. Writing for the court, Laycraft C.J.A. said the question was whether the *Bankruptcy Act* "requires that the assets in the estate of an insolvent well licensee should be distributed to creditors leaving behind the duties respecting environmental safety . . . as a charge to the public" (para. 29). He answered the question in the negative:

The duty is owed as a public duty by all the citizens of the community to their fellow citizens. When the

de nature réglementaire. Elles demeurent en vigueur jusqu'à ce que le site ait été décontaminé ou que l'affaire soit réglée d'une autre façon.

[71] Il n'est pas inhabituel pour les sociétés qui cherchent à se restructurer sous le régime de la *LACC* d'être assujetties à diverses ordonnances réglementaires continues découlant de régimes législatifs régissant des domaines tels que l'emploi, la conservation de l'énergie et l'environnement. La société demeure assujettie à ces exigences alors qu'elle continue d'exercer ses activités pendant la période de restructuration, et elle y demeure assujettie au terme de cette période de restructuration, à moins que ces exigences n'aient fait l'objet d'une transaction ou qu'elles n'aient été liquidées.

[72] La *LACC*, à l'instar de la *Loi sur la faillite et l'insolvabilité*, L.R.C. 1985, ch. B-3 (« *LFI* »), établit une distinction fondamentale entre les exigences réglementaires continues établies en faveur du public, lesquelles continuent de s'appliquer après la restructuration, et les réclamations pécuniaires qui peuvent faire l'objet d'une transaction.

[73] Cette distinction est aussi reconnue dans la jurisprudence, selon laquelle les obligations réglementaires établies en faveur du public ne sont pas des « réclamations » aux termes de la *LFI* ni, par extension, aux termes de la *LACC*. Dans l'arrêt *Panamericana de Bienes y Servicios S.A. c. Northern Badger Oil & Gas Ltd.* (1991), 81 Alta. L.R. (2d) 45, la Cour d'appel de l'Alberta a statué qu'un séquestre doit se conformer à une ordonnance de l'Energy Resources Conservation Board lui enjoignant de respecter des exigences en matière d'abandon de puits. Le juge en chef Laycraft, au nom de la cour, a affirmé que la question à trancher était de savoir si la *Loi sur la faillite* [TRADUCTION] « exige que les actifs se trouvant dans le patrimoine d'un titulaire de permis de puits soient distribués aux créanciers en laissant à la charge du public les obligations en matière de sécurité environnementale » (par. 29). Il a répondu par la négative :

[TRADUCTION] L'obligation est établie comme une obligation à caractère public qui doit être respectée par

citizen subject to the order complies, the result is not the recovery of money by the peace officer or public authority, or of a judgment for money, nor is that the object of the whole process. Rather, it is simply the enforcement of the general law. The enforcing authority does not become a "creditor" of the citizen on whom the duty is imposed. [Emphasis added; para. 33.]

l'ensemble des citoyens de la collectivité à l'égard de leurs concitoyens. Lorsque le citoyen visé par l'ordonnance s'y conforme, le résultat n'est pas perçu comme le recouvrement d'une somme d'argent par un agent de la paix ou l'autorité publique, ni comme l'exécution d'un jugement ordonnant le paiement d'une somme d'argent; d'ailleurs, cela ne constitue pas non plus l'objectif de l'ensemble du processus. Il faut plutôt y voir l'application d'une loi générale. L'organisme d'application de la loi ne devient pas un « créancier » du citoyen à qui incombe l'obligation. [Je souligne; par. 33.]

[74] The distinction between regulatory obligations under the general law aimed at the protection of the public and monetary claims that can be compromised in *CCAA* restructuring or bankruptcy is a fundamental plank of Canadian corporate law. It has been repeatedly acknowledged: *Lamford Forest Products Ltd. (Re)* (1991), 86 D.L.R. (4th) 534 (B.C.S.C.); *Shirley (Re)* (1995), 129 D.L.R. (4th) 105 (Ont. Ct. (Gen. Div.)), at p. 109; *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453, at para. 146, *per* Iacobucci J. (dissenting). As Farley J. succinctly put it in *Air Canada, Re [Regulators' motions]* (2003), 28 C.B.R. (5th) 52 (Ont. S.C.J.), at para. 18: "Once [the company] emerges from these CCAA proceedings (successfully one would hope), then it will have to deal with each and every then unresolved [regulatory] matter."

[74] La distinction entre les exigences réglementaires découlant d'une loi d'application générale visant la protection du public, d'une part, et les réclamations pécuniaires pouvant faire l'objet d'une transaction dans le cadre d'une restructuration engagée sous le régime de la *LACC* ou en matière de faillite, d'autre part, constitue un élément important du droit canadien des sociétés. Cette distinction a maintes fois été reconnue : *Lamford Forest Products Ltd. (Re)* (1991), 86 D.L.R. (4th) 534 (C.S.C.-B.); *Shirley (Re)* (1995), 129 D.L.R. (4th) 105 (C. Ont. (Div. gén.)), p. 109; *Husky Oil Operations Ltd. c. Ministre du Revenu national*, [1995] 3 R.C.S. 453, par. 146, le juge Iacobucci (dissident). Comme l'a dit succinctement le juge Farley dans *Air Canada, Re [Regulators' motions]* (2003), 28 C.B.R. (5th) 52 (C.S.J. Ont.), par. 18 : [TRADUCTION] « À l'issue des procédures engagées en vertu de la LACC — souhaitons qu'elles soient couronnées de succès — [la société] aura alors à régler chacun des dossiers non résolus [en matière réglementaire]. »

[75] Recent amendments to the *CCAA* confirm this distinction. Section 11.1(2) now explicitly provides that, except to the extent a regulator is enforcing a payment obligation, a general stay does not affect a regulatory body's authority in relation to a corporation going through restructuring. The *CCAA* court may only stay specific actions or suits brought by a regulatory body, and only if such action is necessary for a viable compromise to be reached and it would not be contrary to the public interest to make such an order (s. 11.1(3)).

[75] Des modifications apportées récemment à la *LACC* confirment cette distinction. Le paragraphe 11.1(2) prévoit maintenant expressément que, sauf dans la mesure où un organisme de réglementation fait respecter une obligation de paiement, une suspension générale ne porte aucunement atteinte aux pouvoirs de celui-ci à l'égard d'une société en restructuration. Le tribunal chargé d'appliquer la *LACC* ne peut ordonner une suspension qu'à l'égard de certaines actions ou poursuites intentées par un organisme administratif, et seulement si cette mesure est nécessaire à la conclusion d'une transaction viable et si une telle ordonnance ne serait pas contraire à l'intérêt public (par. 11.1(3)).

[76] Abitibi argues that another amendment to the *CCAA*, s. 11.8(9), treats ongoing regulatory duties owed to the public as claims, and erases the distinction between the two types of obligation: see *General Chemical Canada Ltd., Re*, 2007 ONCA 600, 228 O.A.C. 385, *per* Goudge J.A., relying on s. 14.06(8) of the *BIA* (the equivalent of s. 11.8(9) of the *CCAA*). With respect, this reads too much into the provision. Section 11.8(9) of the *CCAA* refers only to the situation where a government has performed remediation, and provides that the *costs of the remediation* become a claim in the restructuring process even where the environmental damage arose after *CCAA* proceedings have begun. As stated in *Strathcona (County) v. PriceWaterhouseCoopers Inc.*, 2005 ABQB 559, 47 Alta. L.R. (4th) 138, *per* Burrows J., the section "does not convert a statutorily imposed obligation owed to the public at large into a liability owed to the public body charged with enforcing it" (para. 42).

[76] Abitibi plaide qu'en vertu d'une autre modification apportée à la *LACC*, le par. 11.8(9), les exigences réglementaires continues établies en faveur du public sont considérées comme des réclamations, et que cette modification élimine la distinction entre les deux types d'obligations : voir *General Chemical Canada Ltd., Re*, 2007 ONCA 600, 228 O.A.C. 385, le juge Goudge, citant le par. 14.06(8) de la *LFI* (la disposition équivalente au par. 11.8(9) de la *LACC*). Avec égards, cette interprétation de la disposition est trop large. Le paragraphe 11.8(9) de la *LACC* vise uniquement la situation où un gouvernement a exécuté des travaux de réparation du dommage, et prévoit que les *frais de réparation* constituent une réclamation dans le cadre du processus de restructuration, même si les dommages ont été causés à l'environnement après l'introduction des procédures au titre de la *LACC*. Comme l'a déclaré le juge Burrows dans *Strathcona (County) c. PriceWaterhouseCoopers Inc.*, 2005 ABQB 559, 47 Alta. L.R. (4th) 138, la disposition [TRADUCTION] « ne convertit pas une exigence imposée par la loi et établie en faveur du public en général en une dette envers l'organisme public chargé d'appliquer la loi » (par. 42).

4. When Does a Regulatory Obligation Become a Claim Under the *CCAA*?

[77] This brings us to the heart of the question before us: When does a regulatory obligation imposed on a corporation under environmental protection legislation become a "claim" provable and compromisable under the *CCAA*?

[78] Regulatory obligations are, as a general proposition, not compromisable claims. Only financial or monetary claims provable by a "creditor" fall within the definition of "claim" under the *CCAA*. A "creditor" is defined as "a person having a claim": s. 2, *BIA*. Thus, the identification of a "creditor" hangs on the existence of a "claim". Section 12(1) of the *CCAA* defines "claim" as "any indebtedness, liability or obligation . . . that . . . would be a debt provable in bankruptcy", which is

4. Quand une exigence réglementaire devient-elle une réclamation au titre de la *LACC*?

[77] Ceci nous amène au cœur de la question dont nous sommes saisis : quand une exigence réglementaire imposée à une société en vertu d'une loi sur la protection de l'environnement devient-elle une « réclamation » prouvable et pouvant faire l'objet d'une transaction aux termes de la *LACC*?

[78] En règle générale, les exigences réglementaires ne sont pas des réclamations pouvant faire l'objet d'une transaction. Seules les réclamations financières ou pécuniaires prouvables par un « créancier » correspondent à la définition de « réclamation » au sens de la *LACC*. Un « créancier » est défini comme étant une « [p]ersonne ayant une réclamation » : art. 2, *LFI*. Ainsi, l'identification d'un « créancier » repose sur l'existence d'une « réclamation ». Le paragraphe 12(1) de la *LACC* définit une « réclamation »

accepted as confined to obligations of a financial or monetary nature.

[79] The *CCAA* does not depart from the proposition that a claim must be financial or monetary. However, it contains a scheme to deal with disputes over whether an obligation is a monetary obligation as opposed to some other kind of obligation.

[80] Such a dispute may arise with respect to environmental obligations of the corporation. The *CCAA* recognizes three situations that may arise when a corporation enters restructuring.

[81] The first situation is where the remedial work has not been done (and there is no "sufficient certainty" that the work will be done, unlike the third situation described below). In this situation, the government cannot claim the cost of remediation: see s. 102(3) of the *EPA*. The obligation of compliance falls in principle on the monitor who takes over the corporation's assets and operations. If the monitor remediates the property, he can claim the costs as costs of administration. If he does not wish to do so, he may obtain a court order staying the remediation obligation or abandon the property: s. 11.8(5) *CCAA* (in which case costs of remediation shall not rank as costs of administration: s. 11.8(7)). In this situation, the obligation cannot be compromised.

[82] The second situation is where the government that has issued the environmental protection order moves to clean up the pollution, as the legislation entitles it to do. In this situation, the government has a claim for the cost of remediation that is compromisable in the *CCAA* proceedings. This is because the government, by moving to clean up the pollution, has changed the outstanding regulatory

comme étant « toute dette, tout engagement ou toute obligation [. . .] qui [. . .] constituerait une dette prouvable en matière de faillite », une définition dont la portée reconnue se limite aux obligations de nature financière ou pécuniaire.

[79] La *LACC* ne s'écarte pas du principe selon lequel une réclamation doit être financière ou pécuniaire. Elle prévoit cependant un régime permettant de régler les différends portant sur la question de savoir si une obligation est de nature pécuniaire, par opposition à une obligation d'une autre nature.

[80] Les obligations environnementales qui incombent à une personne morale peuvent engendrer un tel différend. La *LACC* reconnaît trois situations susceptibles de se présenter lorsqu'une personne morale s'engage dans un processus de restructuration.

[81] La première situation est celle où les travaux de restauration du site n'ont pas été exécutés (et il n'est pas « suffisamment certain » que les travaux seront exécutés, contrairement à la troisième situation exposée ci-après). En pareil cas, le gouvernement ne peut réclamer le coût de la restauration : voir le par. 102(3) de l'*EPA*. En principe, l'obligation de se conformer à la loi incombe au contrôleur qui prend en charge l'actif et les activités de la société. Si le contrôleur exécute les travaux de restauration du site, il peut réclamer les frais en tant que frais d'administration. S'il ne désire pas le faire, il peut obtenir de la cour une ordonnance suspendant l'exigence de restauration ou il peut abandonner l'immeuble : par. 11.8(5) de la *LACC* (dans ce cas, les frais de restauration ne font pas partie des frais d'administration : par. 11.8(7)). En pareil cas, l'obligation ne peut faire l'objet d'une transaction.

[82] La deuxième situation est celle où le gouvernement qui a émis l'ordonnance environnementale prend des mesures de décontamination, ce que la législation l'autorise à faire. En pareil cas, le gouvernement peut produire, pour le coût de la décontamination, une réclamation qui pourra faire l'objet d'une transaction dans le cadre des procédures engagées sous le régime de la *LACC*. Il en est ainsi

obligation owed to the public into a financial or monetary obligation owed by the corporation to the government. Section 11.8(9), already discussed, makes it clear that this applies to damage after the *CCAA* proceedings commenced, which might otherwise not be claimable as a matter of timing.

parce que le gouvernement, en prenant des mesures pour décontaminer le site, a transformé l'exigence réglementaire non exécutée établie en faveur du public en une obligation financière ou pécuniaire à laquelle la société est tenue envers le gouvernement. Le paragraphe 11.8(9), examiné précédemment, prévoit clairement que cette situation s'applique aux dommages survenus après que les procédures ont été engagées au titre de la *LACC*; en l'absence d'une telle précision, ces dommages ne pourraient faire l'objet d'une réclamation compte tenu du moment choisi pour agir.

[83] A third situation may arise: the government has not yet performed the remediation at the time of restructuring, but there is "sufficient certainty" that it will do so. This situation is regulated by the provisions of the *CCAA* for contingent or future claims. Under the *CCAA*, a debt or liability that is contingent on a future event may be compromised.

[83] Une troisième situation peut se présenter : le gouvernement n'a pas encore exécuté des travaux de restauration au moment de la restructuration, mais il est « suffisamment certain » qu'il le fera. Cette situation est prévue par les dispositions de la *LACC* relatives aux réclamations éventuelles ou futures. Aux termes de la *LACC*, une dette ou un engagement qui dépend d'un événement futur peut faire l'objet d'une transaction.

[84] It is clear that a mere possibility that work will be done does not suffice to make a regulatory obligation a contingent claim under the *CCAA*. Rather, there must be "sufficient certainty" that the obligation will be converted into a financial or monetary claim to permit this. The impact of the obligation on the insolvency process is irrelevant to the analysis of contingency. The future liabilities must not be "so remote and speculative in nature that they could not properly be considered contingent claims": *Confederation Treasury Services Ltd. (Bankrupt), Re* (1997), 96 O.A.C. 75, at para. 4.

[84] Il est évident qu'une simple possibilité que les travaux soient exécutés ne suffit pas pour transformer une exigence réglementaire en une réclamation éventuelle au titre de la *LACC*. Pour en arriver à ce résultat, il faut plutôt qu'il soit « suffisamment certain » que l'exigence sera convertie en une réclamation financière ou pécuniaire. L'incidence de l'exigence sur le processus d'insolvabilité n'est pas pertinente pour l'analyse du caractère éventuel de la réclamation. Les engagements futurs ne doivent pas être [TRADUCTION] « si lointains et hypothétiques qu'ils ne puissent être considérés à bon droit comme des réclamations éventuelles » : *Confederation Treasury Services Ltd. (Bankrupt), Re* (1997), 96 O.A.C. 75, par. 4.

[85] Where environmental obligations are concerned, courts to date have relied on a high degree of probability verging on certainty that the government will in fact step in and remediate the property. In *Anvil Range Mining Corp., Re* (2001), 25 C.B.R. (4th) 1 (Ont. S.C.J.), Farley J. concluded that a contingent claim was established where the money had already been earmarked in the budget for the remediation project. He observed that

[85] Lorsque des exigences environnementales sont en cause, les tribunaux se sont jusqu'à ce jour fondés sur un haut degré de probabilité, proche de la certitude, que le gouvernement prendra réellement des mesures et exécutera les travaux de restauration. Dans *Anvil Range Mining Corp., Re* (2001), 25 C.B.R. (4th) 1 (C.S.J. Ont.), le juge Farley a conclu que la preuve d'une réclamation éventuelle était établie parce que les fonds avaient

"there appears to be every likelihood to a certainty that every dollar in the budget for the year ending March 31, 2002 earmarked for reclamation will be spent" (para. 15 (emphasis added)). Similarly, in *Shirley (Re)*, Kennedy J. relied on the fact that the Ontario Minister of the Environment had already entered the property at issue and commenced remediation activities to conclude that "[a]ny doubt about the resolve of the [Ministry's] intent to realize upon its authority ended when it began to incur expense from operations" (p. 110).

déjà été dédiés au projet de restauration dans le budget. Il a fait remarquer qu'[TRADUCTION] « il semble fortement probable et presque certain que chaque dollar dédié aux réclamations figurant au budget établi pour l'année se terminant le 31 mars 2002 sera dépensé » (par. 15 (je souligne)). De même, dans *Shirley (Re)*, le juge Kennedy s'est fondé sur le fait que les employés du ministère de l'Environnement de l'Ontario se trouvaient déjà sur le terrain en cause et avaient commencé les travaux de restauration pour conclure que [TRADUCTION] « [t]ous doutes quant à la détermination du [ministère] d'exercer son droit se sont estompés lorsque l'opération a commencé à lui occasionner des dépenses » (p. 110).

[86] There is good reason why "sufficient certainty" should be interpreted as requiring "likelihood approaching certainty" when the issue is whether ongoing environmental obligations owed to the public should be converted to contingent claims that can be expunged or compromised in the restructuring process. Courts should not overlook the obstacles governments may encounter in deciding to remediate environmental damage a corporation has caused. To begin with, the government's decision is discretionary and may be influenced by any number of competing political and social considerations. Furthermore, remediation may cost a great deal of money. For example, in this case, the *CCAA* court found that at a minimum the remediation would cost in the "mid-to-high eight figures", and could indeed cost several times that (para. 81). In concrete terms, the remediation at issue in this case may be expected to meet or exceed the entire budget of the Minister ($65 million) for 2009. Not only would this be a massive expenditure, but it would also likely require the specific approval of the legislature and thereby be subject to political uncertainties. To assess these factors and determine whether all this will occur would embroil the *CCAA* judge in social, economic and political considerations — matters which are not normally subject to judicial consideration: *R. v. Imperial Tobacco Canada Ltd.*, 2011 SCC 42, [2011] 3 S.C.R. 45, at para. 74. It is small wonder, then, that courts assessing whether it is "sufficiently certain" that a government will clean up pollution created

[86] Une bonne raison explique pourquoi il convient d'interpréter l'expression « suffisamment certain » comme exigeant une « probabilité proche de la certitude » lorsqu'il s'agit de déterminer si des exigences environnementales continues établies en faveur du public devraient être converties en réclamations éventuelles qui peuvent être rayées ou faire l'objet d'une transaction dans le cadre du processus de restructuration. Les tribunaux ne devraient pas oublier les obstacles auxquels les gouvernements peuvent se heurter lorsqu'ils décident de réparer les dommages environnementaux causés par une société. D'abord, la décision du gouvernement est discrétionnaire, et elle peut être influencée par nombre de considérations politiques et sociales concurrentes. En outre, les travaux de restauration peuvent être très coûteux. En l'espèce, par exemple, le juge de première instance a conclu que ces travaux pourraient coûter au minimum [TRADUCTION] « entre cinquante et cent millions de dollars », et même plusieurs fois cette somme (par. 81). En termes concrets, le coût des travaux en cause en l'espèce pourrait atteindre ou dépasser le budget total du ministre (65 millions de dollars) pour l'exercice 2009. Il s'agirait non seulement d'une dépense énorme, mais il faudrait probablement aussi l'approbation explicite de l'assemblée législative, avec les incertitudes politiques que cela comporte. L'évaluation de ces facteurs et l'appréciation de la possibilité que tout ce qui précède se produise entraîneraient le juge chargé d'appliquer la *LACC* dans des considérations d'ordre

by a corporation have insisted on proof of likelihood approaching certainty.

[87] In this case, as will be seen, apart from the Buchans property, the record is devoid of any evidence capable of establishing that it is "sufficiently certain" that the Province will itself remediate the properties. Even on a more relaxed standard than the one adopted in similar cases to date, the evidence in this case would fail to establish that remediation is "sufficiently certain".

5. The Result in This Case

[88] Five different sites are at issue in this case. The question in each case is whether the Minister has already remediated the property (making it to that extent an actual claim), or if not, whether it is "sufficiently certain" that he or she will remediate the property, permitting it to be considered a contingent claim.

[89] The Buchans site posed immediate risks to human health as a consequence of high levels of lead and other contaminants in the soil, groundwater, surface water and sediment. There was a risk that the wind would disperse the contamination, posing a threat to the surrounding population. Lead has been found in residential areas of Buchans and adults tested in the town had elevated levels of lead in their blood. In addition, a structurally unsound dam at the Buchans site raised the risk of contaminating silt entering the Exploits and Buchans rivers.

[90] The Minister quickly moved to address the immediate concern of the unsound dam and put

social, économique et politique — des questions normalement soustraites à l'examen judiciaire : *R. c. Imperial Tobacco Canada Ltée*, 2011 CSC 42, [2011] 3 R.C.S. 45, par. 74. Il n'est donc pas étonnant que les tribunaux, lorsqu'il s'agit d'apprécier s'il est « suffisamment certain » qu'un gouvernement procédera à la décontamination causée par une société, s'en soient tenus à la preuve d'une probabilité proche de la certitude.

[87] En l'espèce, comme nous le verrons, à l'exclusion du site de Buchans, le dossier est dénué d'éléments de preuve susceptibles d'établir qu'il est « suffisamment certain » que la province exécutera elle-même les travaux de décontamination. Même si l'on applique une norme plus souple que celle retenue jusqu'à ce jour dans des affaires semblables, la preuve en l'espèce n'établirait pas qu'il est « suffisamment certain » que les sites seront décontaminés.

5. L'issue du présent pourvoi

[88] En l'espèce, cinq sites différents sont en cause. La question dans chaque cas est de savoir si le ministre a déjà décontaminé les sites — il aurait alors une réclamation — ou, si tel n'est pas le cas, s'il est « suffisamment certain » qu'il exécutera les travaux de restauration, ce qui permettrait de considérer le coût de la décontamination comme une réclamation éventuelle.

[89] Le site de Buchans posait un risque immédiat à la santé pour les humains en raison de la forte concentration de plomb et d'autres contaminants présente dans le sol, l'eau souterraine et de surface ainsi que dans des sédiments. Il y avait un risque que le vent disperse la contamination, ce qui aurait représenté une menace pour la population environnante. On a trouvé du plomb dans des zones résidentielles de Buchans et les tests de sang ont révélé chez des adultes résidant dans la ville des concentrations élevées de plomb. De plus, un barrage en mauvais état situé sur le site de Buchans augmentait le risque de contamination du limon se déversant dans les rivières Exploits et Buchans.

[90] La ministre de l'époque a rapidement pris des mesures pour régler le problème immédiat du

out a request for tenders for other measures that required immediate action at the Buchans site. Money expended is clearly a claim under the *CCAA*. I am also of the view that the work for which the request for tenders was put out meets the "sufficiently certain" standard and constitutes a contingent claim.

[91] Beyond this, it has not been shown that it is "sufficiently certain" that the Province will do the remediation work to permit Abitibi's ongoing regulatory obligations under the *EPA* Orders to be considered contingent debts. The same applies to the other properties, on which no work has been done and no requests for tender to do the work initiated.

[92] Far from being "sufficiently certain", there is simply nothing on the record to support the view that the Province will move to remediate the remaining properties. It has not been shown that the contamination poses immediate health risks, which must be addressed without delay. It has not been shown that the Province has taken any steps to do any work. And it has not been shown that the Province has set aside or even contemplated setting aside money for this work. Abitibi relies on a statement by the then-Premier in discussing the possibility that the Province would be obliged to compensate Abitibi for expropriation of some of the properties, to the effect that "there would not be a net payment to Abitibi": R.F., at para. 12. Apart from the fact that the Premier was not purporting to state government policy, the statement simply does not say that the Province would do the remediation. The Premier may have simply been suggesting that outstanding environmental liabilities made the properties worth little or nothing, obviating any net payment to Abitibi.

[93] My colleague Deschamps J. concludes that the findings of the *CCAA* court establish that it was

barrage en mauvais état et a lancé un appel d'offres relatif aux autres mesures nécessitant une intervention immédiate sur le site de Buchans. Il est clair que les sommes d'argent dépensées constituent une réclamation au sens de la *LACC*. J'estime également que les travaux à l'égard desquels des appels d'offres ont été lancés satisfont à la norme de ce qui est « suffisamment certain » et qu'ils constituent une réclamation éventuelle.

[91] Quant au reste, on n'a pas établi qu'il soit « suffisamment certain » que la province exécutera les travaux de décontamination de façon à pouvoir considérer comme des dettes éventuelles les exigences réglementaires continues que les ordonnances *EPA* ont imposées à Abitibi. La même conclusion s'applique à l'égard des autres sites, où aucun travail n'a été réalisé et pour lesquels aucun appel d'offres n'a été lancé pour l'exécution des travaux.

[92] Il n'est pas « suffisamment certain » que la province entreprenne la décontamination des autres sites : aucune preuve au dossier ne laisse entrevoir cette possibilité. Il n'a pas été démontré que la contamination pose pour la santé des risques immédiats exigeant la prise de mesures dans les plus brefs délais. Il n'a pas été démontré que la province a pris quelque mesure que ce soit pour réaliser des travaux. Et il n'a pas été démontré que la province a prévu des sommes d'argent pour ces travaux ou qu'elle a même songé à en prévoir. Abitibi se fonde sur une déclaration du premier ministre de l'époque, qui examinait la possibilité que la province soit tenue de verser à Abitibi une indemnité pour l'expropriation de certains terrains, selon laquelle [TRADUCTION] « aucun montant net ne serait versé à Abitibi » : m.i., par. 12. Mis à part le fait que le premier ministre ne prétendait pas établir une politique gouvernementale, sa déclaration n'indique aucunement que la province exécuterait la décontamination. Le premier ministre indiquait peut-être simplement qu'en raison des exigences environnementales non respectées, les terrains ne valaient plus rien ou presque et qu'il serait inutile de verser quoi que ce soit à Abitibi.

[93] Ma collègue la juge Deschamps conclut que les constatations du juge de première instance

"sufficiently certain" that the Province would remediate the land, converting Abitibi's regulatory obligations under the *EPA* Orders to contingent claims that can be compromised under the *CCAA*. With respect, I find myself unable to agree.

[94] The *CCAA* judge never asked himself the critical question of whether it was "sufficiently certain" that the Province would do the work itself. Essentially, he proceeded on the basis that the *EPA* Orders had not been put forward in a sincere effort to obtain remediation, but were simply a money grab. The *CCAA* judge buttressed his view that the Province's regulatory orders were not sincere by opining that the orders were unenforceable (which if true would not prevent new *EPA* orders) and by suggesting that the Province did not want to assert a contingent claim, since this might attract a counterclaim by Abitibi for the expropriation of the properties (something that may be impossible due to Abitibi's decision to take the expropriation issue to NAFTA (the *North American Free Trade Agreement Between the Government of Canada, the Government of the United Mexican States and the Government of the United States of America*, Can. T.S. 1994 No. 2), excluding Canadian courts). In any event, it is clear that the *CCAA* judge, on the reasoning he adopted, never considered the question of whether it was "sufficiently certain" that the Province would remediate the properties. It follows that the *CCAA* judge's conclusions cannot support the view that the outstanding obligations are contingent claims under the *CCAA*.

[95] My colleague concludes:

[The *CCAA* judge] did at times rely on indicators that are unique and that do not appear in the analytical framework I propose above, but he did so because of the exceptional facts of this case. Yet, had he formulated the

établissent qu'il est « suffisamment certain » que la province décontaminerait les terrains, transformant ainsi les exigences réglementaires que les ordonnances *EPA* imposent à Abitibi en réclamations éventuelles pouvant faire l'objet d'une transaction sous le régime de la *LACC*. Avec égards, je ne puis souscrire à cette conclusion.

[94] Le juge de première instance ne s'est jamais posé la question cruciale de savoir s'il était « suffisamment certain » que la province exécuterait elle-même les travaux. Essentiellement, il a tenu pour acquis que les ordonnances *EPA* n'avaient pas été émises avec l'intention sincère d'obtenir la décontamination des sites, mais qu'il s'agissait simplement d'une manœuvre pour soutirer de l'argent. Le juge a renforcé son point de vue selon lequel les ordonnances réglementaires émises par la province étaient dépourvues de sincérité en exprimant l'avis qu'elles n'étaient pas susceptibles d'exécution (ce qui, si cela s'avérait exact, n'empêcherait pas que de nouvelles ordonnances soient émises). Le juge a également laissé entendre que la province ne voulait pas produire une réclamation éventuelle, ce qui aurait pu provoquer le dépôt d'une demande reconventionnelle d'Abitibi pour l'expropriation des propriétés (un résultat qui peut s'avérer impossible étant donné la décision d'Abitibi de soumettre la question de l'expropriation à l'ALÉNA (*Accord de libre-échange nord-américain entre le gouvernement du Canada, le gouvernement des États-Unis d'Amérique et le gouvernement des États-Unis du Mexique*, R.T. Can. 1994 n^{o} 2), en écartant la juridiction des tribunaux canadiens). Quoi qu'il en soit, il est évident que dans son raisonnement, le juge de première instance n'a jamais examiné la question de savoir s'il était « suffisamment certain » que la province décontaminerait les sites. Il s'ensuit que les conclusions du juge ne peuvent soutenir le point de vue selon lequel les obligations non exécutées constituent des réclamations éventuelles au sens de la *LACC*.

[95] Ma collègue conclut comme suit :

À l'occasion, [le juge] s'est appuyé sur des indicateurs singuliers qui ne figurent pas dans le cadre analytique que j'ai déjà proposé, mais cela s'explique par les faits exceptionnels en l'espèce. Or, s'il avait formulé la question

question in the same way as I have, his conclusion, based on his objective findings of fact, would have been the same. . . . The *CCAA* judge's assessment of the facts . . . leads to no conclusion other than that it was sufficiently certain that the Province would perform remediation work and therefore fall within the definition of a creditor with a monetary claim. [Emphasis added; para. 58.]

[96] I must respectfully confess to a less sanguine view. First, I find myself unable to decide the case on what I think the *CCAA* judge would have done had he gotten the law right and considered the central question. In my view, his failure to consider that question requires this Court to answer it in his stead on the record before us: *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235, at para. 35. But more to the point, I see no objective facts that support, much less compel, the conclusion that it is "sufficiently certain" that the Province will move to itself remediate any or all of the pollution Abitibi caused. The mood of the regulator in issuing remediation orders, be it disinterested or otherwise, has no bearing on the likelihood that the Province will undertake such a massive project itself. The Province has options. It could, to be sure, opt to do the work. Or it could await the result of Abitibi's restructuring and call on it to remediate once it resumed operations. It could even choose to leave the sites contaminated. There is nothing in the record that makes the first option more probable than the others, much less establishes "sufficient certainty" that the Province will itself clean up the pollution, converting it to a debt.

[97] I would allow the appeal and issue a declaration that Abitibi's remediation obligations under the *EPA* Orders do not constitute claims compromisable under the *CCAA*, except for work done or tendered for on the Buchans site.

comme je l'ai posée, sa conclusion, appuyée sur ses constatations de fait objectives, aurait été la même. [. . .] L'appréciation des faits par le juge [. . .] ne permet de tirer aucune conclusion autre que celle suivant laquelle il était suffisamment certain que la province exécuterait des travaux de décontamination et qu'elle était par conséquent visée par la définition d'un créancier ayant une réclamation pécuniaire. [Je souligne; par. 58.]

[96] Avec égards, je dois avouer que je ne partage pas la certitude de ma collègue à ce titre. Premièrement, j'estime ne pas pouvoir trancher le pourvoi en me fondant sur ce que je crois qu'aurait fait le juge de première instance s'il avait alors saisi correctement le droit et examiné la question réellement en jeu. À mon avis, le fait qu'il n'ait pas examiné cette question oblige notre Cour à y répondre à sa place au vu du dossier : *Housen c. Nikolaisen*, 2002 CSC 33, [2002] 2 R.C.S. 235, par. 35. Mais, plus précisément, je ne vois pas de faits objectifs qui appuient, et encore moins qui imposent, la conclusion selon laquelle il est « suffisamment certain » que la province entreprendra elle-même de décontaminer un site ou tous les sites pollués par Abitibi. L'humeur de l'organisme de réglementation qui ordonne la décontamination, qu'il soit ou non désintéressé, n'a aucune incidence sur la probabilité que la province entreprenne elle-même un projet d'une telle ampleur. Des choix s'offrent à la province. Elle pourrait certes choisir d'exécuter les travaux. Ou elle pourrait attendre le résultat de la restructuration d'Abitibi et lui demander d'exécuter les travaux d'assainissement une fois qu'elle aura repris ses activités. Elle pourrait même choisir de laisser les sites contaminés. Rien au dossier n'indique que le premier choix est plus susceptible d'être retenu que les autres, et encore moins qui établisse qu'il est « suffisamment certain » que la province exécutera elle-même la décontamination, convertissant ainsi l'opération en une créance.

[97] Je suis d'avis d'accueillir le pourvoi et de déclarer que les obligations de décontaminer les sites qui incombent à Abitibi aux termes des ordonnances *EPA* ne constituent pas des réclamations pouvant faire l'objet d'une transaction aux termes de la *LACC*, à l'exception des travaux exécutés sur le site de Buchans ou à l'égard desquels des appels d'offres ont été lancés.

The following are the reasons delivered by

[98] LeBel J. (dissenting) — I have read the reasons of the Chief Justice and Deschamps J. They agree that a court overseeing a proposed arrangement under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"), cannot relieve debtors of their regulatory obligations. The only regulatory orders that can be subject to compromise are those which are monetary in nature. My colleagues also accept that contingent environmental claims can be liquidated and compromised if it is established that the regulatory body would remediate the environmental contamination itself, and hence turn the regulatory order into a monetary claim.

[99] At this point, my colleagues disagree on the proper evidentiary test with respect to whether the government would remediate the contamination. In the Chief Justice's opinion, the evidence must show that there is a "likelihood approaching certainty" that the province would remediate the contamination itself (para. 86). In my respectful opinion, this is not the established test for determining where and how a contingent claim can be liquidated in bankruptcy and insolvency law. The test of "sufficient certainty" described by Deschamps J., which does not look very different from the general civil standard of probability, better reflects how both the common law and the civil law view and deal with contingent claims. On the basis of the test Deschamps J. proposes, I must agree with the Chief Justice and would allow the appeal.

[100] First, no matter how I read the *CCAA* court's judgment (2010 QCCS 1261, 68 C.B.R. (5th) 1), I find no support for a conclusion that it is consistent with the principle that the *CCAA* does not apply to purely regulatory obligations, or that the court had evidence that would satisfy the test of "sufficient certainty" that the province of Newfoundland and

Version française des motifs rendus par

[98] Le juge LeBel (dissident) — J'ai pris connaissance des motifs de la Juge en chef et de la juge Deschamps. Elles s'entendent pour affirmer qu'un tribunal qui supervise un arrangement proposé aux termes de la *Loi sur les arrangements avec les créanciers des compagnies*, L.R.C. 1985, ch. C-36 (« *LACC* »), ne peut soustraire les débiteurs aux exigences réglementaires qui leurs sont imposées. Seules peuvent faire l'objet d'une transaction les ordonnances réglementaires de nature pécuniaire. Mes collègues reconnaissent également que les réclamations environnementales éventuelles peuvent être liquidées ou faire l'objet d'une transaction s'il est établi que l'organisme administratif se chargerait de la décontamination, transformant ainsi l'ordonnance réglementaire en une réclamation pécuniaire.

[99] Sur ce, mes collègues diffèrent d'opinion quant au critère de preuve applicable pour déterminer si le gouvernement entend effectuer la décontamination. De l'avis de la Juge en chef, la preuve doit démontrer une « probabilité proche de la certitude » que la province se chargerait de la décontamination (par. 86). À mon humble avis, il ne s'agit pas du critère établi pour déterminer si, et de quelle façon, une réclamation éventuelle peut être liquidée en droit de la faillite et de l'insolvabilité. Le critère de ce qui est « suffisamment certain » qu'énonce la juge Deschamps ne semble pas différer beaucoup de la norme générale de probabilité en matière civile et reflète mieux la façon dont la common law et le droit civil envisagent et traitent les réclamations éventuelles. Cependant, en appliquant le critère que propose la juge Deschamps, je dois souscrire aux motifs de la Juge en chef et je suis d'avis d'accueillir le pourvoi.

[100] Tout d'abord, sans égard à la façon d'envisager le jugement du tribunal chargé d'appliquer la *LACC* (2010 QCCS 1261, 68 C.B.R. (5th) 1), rien à mon sens ne permet de conclure qu'il soit conforme au principe selon lequel la *LACC* ne s'applique pas aux exigences purement réglementaires, ou que la preuve faite devant le tribunal respecterait le critère

Labrador ("Province") would perform the remedial work itself.

[101] In my view, the *CCAA* court was concerned that the arrangement would fail if the Abitibi respondents ("Abitibi") were not released from their regulatory obligations in respect of pollution. The *CCAA* court wanted to eliminate the uncertainty that would have clouded the reorganized corporations' future. Moreover, its decision appears to have been driven by an opinion that the Province had acted in bad faith in its dealings with Abitibi both during and after the termination of its operations in the Province. I agree with the Chief Justice that there is no evidence that the Province intends to perform the remedial work itself. In the absence of any other evidence, an offhand comment made in the legislature by a member of the government hardly satisfies the "sufficient certainty" test. Even if the evidentiary test proposed by my colleague Deschamps J. is applied, this Court can legitimately disregard the *CCAA* court's finding as the Chief Justice proposes, since it did not rest on a sufficient factual foundation.

[102] For these reasons, I would concur with the disposition proposed by the Chief Justice.

Appeal dismissed with costs, McLachlin C.J. *and* LeBel J. *dissenting.*

Solicitors for the appellant: WeirFoulds, Toronto; Attorney General of Newfoundland and Labrador, St. John's.

Solicitors for the respondents AbitibiBowater Inc., Abitibi-Consolidated Inc. and Bowater Canadian Holdings Inc.: Stikeman Elliott, Toronto.

Solicitors for the respondent the Ad Hoc Committee of Bondholders: Goodmans, Toronto.

Solicitors for the respondents the Ad Hoc Committee of Senior Secured Noteholders and the U.S. Bank National Association (Indenture Trustee

voulant qu'il soit « suffisamment certain » que la province de Terre-Neuve-et-Labrador (« province ») exécuterait elle-même les travaux de décontamination.

[101] À mon avis, le tribunal de première instance craignait un échec de l'arrangement si les sociétés du groupe Abitibi intimées (« Abitibi ») ne pouvaient se libérer des exigences réglementaires relatives à la pollution. Le tribunal voulait écarter l'incertitude qui aurait assombri l'avenir de ces sociétés après leur réorganisation. De plus, sa décision semble motivée par l'opinion suivant laquelle la province avait traité de mauvaise foi avec Abitibi dès que cette dernière eût cessé ses activités dans cette province. Je suis d'accord avec la Juge en chef pour conclure qu'aucune preuve ne confirme l'intention de la province d'exécuter elle-même les travaux de décontamination. En l'absence de tout autre élément de preuve, une remarque faite en passant par un ministre devant l'assemblée législative peut difficilement satisfaire au critère de ce qui est « suffisamment certain ». Même si l'on applique le critère de preuve que propose ma collègue la juge Deschamps, notre Cour peut légitimement écarter les conclusions du tribunal de première instance comme le propose la Juge en chef car elles ne reposent sur aucun fondement factuel suffisant.

[102] Pour ces motifs, je suis d'avis de souscrire au dispositif que propose la Juge en chef.

Pourvoi rejeté avec dépens, la juge en chef McLachlin *et le juge* LeBel *sont dissidents.*

Procureurs de l'appelante : WeirFoulds, Toronto; procureur général de Terre-Neuve-et-Labrador, St. John's.

Procureurs des intimées AbitibiBowater Inc., Abitibi-Consolidated Inc. et Bowater Canadian Holdings Inc. : Stikeman Elliott, Toronto.

Procureurs de l'intimé le comité ad hoc des créanciers obligataires : Goodmans, Toronto.

Procureurs des intimés le comité ad hoc des porteurs de billets garantis de premier rang et U.S. Bank National Association (fiduciaire

for the Senior Secured Noteholders): Borden Ladner Gervais, Toronto.

Solicitor for the intervener the Attorney General of Canada: Attorney General of Canada, Ottawa.

Solicitor for the intervener the Attorney General of Ontario: Attorney General of Ontario, Toronto.

Solicitor for the interveners the Attorney General of British Columbia and Her Majesty The Queen in Right of British Columbia: Attorney General of British Columbia, Victoria.

Solicitor for the intervener the Attorney General of Alberta: Attorney General of Alberta, Edmonton.

Solicitors for the intervener Ernst & Young Inc., as Monitor: Thornton Grout Finnigan, Toronto.

Solicitors for the intervener the Friends of the Earth Canada: Ecojustice, University of Ottawa, Ottawa; Fasken Martineau DuMoulin, Toronto.

désigné par l'acte constitutif pour les porteurs de billets garantis de premier rang) : Borden Ladner Gervais, Toronto.

Procureur de l'intervenant le procureur général du Canada : Procureur général du Canada, Ottawa.

Procureur de l'intervenant le procureur général de l'Ontario : Procureur général de l'Ontario, Toronto.

Procureur des intervenants le procureur général de la Colombie-Britannique et Sa Majesté la Reine du chef de la Colombie-Britannique : Procureur général de la Colombie-Britannique, Victoria.

Procureur de l'intervenant le procureur général de l'Alberta : Procureur général de l'Alberta, Edmonton.

Procureurs de l'intervenante Ernst & Young Inc., en sa qualité de contrôleur : Thornton Grout Finnigan, Toronto.

Procureurs de l'intervenante Les Ami(e)s de la Terre Canada : Ecojustice, Université d'Ottawa, Ottawa; Fasken Martineau DuMoulin, Toronto.

TAB 9

Noble v. Principal Consultants Ltd. (Bankrupt), 2000 ABCA 133

Date: 20000510
Docket: 18436

IN THE COURT OF APPEAL OF ALBERTA

THE COURT:

THE HONOURABLE MADAM JUSTICE PICARD
THE HONOURABLE MR. JUSTICE BERGER
THE HONOURABLE MR. JUSTICE WITTMANN

BETWEEN:

WALLACE H. NOBLE

Appellant

- and-

KPMG INC. AS TRUSTEES IN BANKRUPTCY
OF PRINCIPAL CONSULTANTS LTD.

Respondent

APPEAL FROM THE JUDGMENT OF THE
HONOURABLE MR. JUSTICE R.P. FRASER
DATED AUGUST 5, 1999

REASONS FOR JUDGMENT RESERVED

REASONS FOR JUDGMENT OF THE HONOURABLE MADAM JUSTICE PICARD
CONCURRED IN BY THE HONOURABLE MR. JUSTICE WITTMANN

REASONS FOR JUDGMENT OF THE HONOURABLE MR. JUSTICE BERGER

DISSENTING IN PART

COUNSEL:

W.S. McKall
For the Appellant

L. Robinson
For the Respondent

REASONS FOR JUDGMENT OF THE
HONOURABLE MADAM JUSTICE PICARD

Introduction

[1] This appeal raises the issue of whether the bankruptcy of an employer, after it has wrongfully terminated an employment contract with an employee, affects the quantum of damages to which the employee is entitled.

[2] The appellant, Noble, was employed by Principal Consultants Ltd. (Principal) for over 18 years. At the time of his termination, in August of 1987, he was Senior Vice-President, Finance, Prairie Region. He was terminated without cause and without notice or compensation. In October of 1987, Principal made an assignment in bankruptcy. KPMG Inc., (KPMG) became the trustee in bankruptcy and is the respondent in this action.

[3] There was an agreed statement of facts which included the following:

> (a) the appellant was entitled at common law to 18 months' notice of termination, or payment in lieu thereof;
>
> (b) the appellant's salary was based on the following formula:
>
> > (i) base salary of $5,000 per month,
> > (ii) bonuses calculated on the basis of increased sales in his region.

[4] KPMG takes the position that a bankruptcy limits the quantum of common law damages because, upon that event, Noble would no longer have been employed by Principal. That is, KPMG says that the notice period is reduced to 2 months and 6 days. In support, it refers to the results in cases where employees have become disabled or died after being unlawfully dismissed and to statements in *Dunlop* v. *British Columbia Hydro and Power Authority*, [1988] 32 B.C.L.R. 334 (2d) (B.C.C.A.) and *Rizzo and Rizzo Shoes (Re),* [1998] 1 S.C.R. 27.

[5] Noble argues that upon Principal unlawfully dismissing him, Principal breached its contract with him and he became entitled, at common law, to damages equivalent to 18 months' compensation. Noble says Principal's bankruptcy is not an event that reduces that quantum, that the proper quantification of his common law damages against the bankrupt is compensation based on 18 months' notice, and that he has the right to file a claim for those damages as an unsecured creditor of Principal. Noble distinguishes the disabled/death cases and says the analysis in *Dunlop* and statements in *Rizzo* support his case.

[6] The chambers judge agreed with KPMG. While he distinguished the disabled/death cases, he found support for his conclusion in both the *Dunlop* and *Rizzo* cases.

The Law

[7] Upon a breach of contract, the injured party is entitled to damages to place him, so far as possible, in the same position he would have been if the contract had been performed. *Wertheim* v. *Chicoutimi Pulp Co.*, [1911] A.C. 301.

[8] In an employment contract, there is an implied term that an employer will give an employee reasonable notice of termination. The employee may be given the opportunity to work until the end of the period of notice (working notice) or, he may be given damages in lieu of notice if dismissed summarily without just cause (unlawful dismissal). In the latter case, the dismissed employee has the responsibility of mitigating the loss. *Bardal* v. *Globe & Mail Ltd.*, [1960] O.W.N. 253 (Ont. H.C.)

[9] The general rule regarding damages for breach of contract is that damages are assessed at the date of breach. Fridman, *The Law of Contract*, 3rd ed. (Scarborough, Ontario: Carswell, 1994), at p. 754. Over the years qualifications have been made to this rule, for example, in cases involving the sale of goods or land where specific performance may be in issue and price fluctuations could greatly affect damages. See, *Johnson* v. *Agnew*, [1980] A.C. 367 (H.L.); *Asamera Oil Corp. Ltd.* v. *Sea Oil and General Corp*, [1979] 1 S.C.R. 633. No factors justifying a qualification are present in this case, thus the general rule would apply.

[10] When assessing damages for breach of contract, two distinct issues arise, remoteness and quantification. See Fridman, at p.711. Remoteness is a question of whether the damage suffered is properly recoverable in an action for breach of contract. The test for remoteness is founded in *Hadley* v. *Baxendale*, (1854) 156 E.R. 145 (Ex.) which says that damages for breach of contract are limited to the ordinary natural consequences of a breach or for consequences that might reasonably have been in the contemplation of both parties when they made the contract. See Fridman, p. 712. In the case of the breach of a contract of employment, damages in lieu of notice are not too remote.

[11] Quantifying damages often presents a challenge because of a myriad of factors and forces, including the intention of the parties and events subsequent to the contract. In this case, KPMG raises the bankruptcy of the employer as a basis for terminating the common law notice period as of the date of the bankruptcy. KPMG also seeks to reduce the quantum of the award by challenging the bonus portion of the salary payment that is based on sales.

[12] It appears that there are no reported cases considering the effect of a subsequent bankruptcy of the employer on common law damages for unlawful dismissal.

[13] In the *Dunlop* case, after being terminated without cause and without notice, the employee suffered an injury that disabled him for 12 months. The trial judge found that reasonable notice was 20 months but deducted 12 months on the basis that the employer would

not have paid him for that period, had he been in its employment on a working notice basis. (It appears that the employee would have been paid during that time by a disability plan.) Writing for the British Columbia Court of Appeal, Justice Lambert reversed that decision on the basis that the employee's disability did not have any effect on the period of reasonable notice. He found it was not a factor that should reduce the quantum of the claim, which was based on compensation equivalent to 20 months' salary.

[14] In a contract of employment, there is an implied term that each party must give reasonable notice to the other. There is **not** an implied term that the employer may pay damages in lieu of notice. The employee is entitled to damages because the employer is liable to the employee for breaching the implied term that it must give reasonable notice. The employer cannot characterize such a payment as compliance with an implied term that it can breach the contract so long as it pays because there is no such implied term.

[15] The issue in *Dunlop* was the effect to be given to an event that occurred after the dismissal and that would have prevented the dismissed employee from earning income if he had remained as an employee serving out a working notice. Justice Lambert's statements about the effect to be given to such subsequent events were relied on by the chambers judge in this case.

[16] Justice Lambert said in *Dunlop*, at p.339;

> ...in considering the significance of events following the dismissal, the proper principle, in my opinion, is that *an event* which occurs after a wrongful dismissal and before trial, or before the end of the notice period, whichever comes first, *may be considered in assessing damages actually suffered* by the dismissed employee. The legal significance to be attached to the event will depend on the nature of the event and on other relevant factors in the case. *But, to the extent that the damages are derived from a determination of the proper notice period, that notice period is determinable once and for all at the time of the breach of the contract and is not, itself, affected by subsequent events.*
>
> (emphasis supplied)

[17] In applying his test, Justice Lambert concluded that the employee's disability did not have any effect on the period of reasonable notice because the employer, who had breached the contract, could not rely on the employee's disability to diminish or deny his claim. Specifically, Justice Lambert refused to apply the "working notice" model to the breach situation. He found that after the breach of contract, the subsequent events were of no consequence. He said that when the employer broke the contract it lost its right to rely on the provision in the contract that no salary would be paid with respect to a period of disability.

[18] In summary, Justice Lambert held that the notice period is to be determined at the time of the breach and is not affected by subsequent events. He left the door open for the consideration of an event in assessing *damages actually suffered* in so far as they are not derived from a notice period. In the case before him, however, he did not accept the employer's argument that, because it would not have had to pay the employee during a period that he was disabled had he been given working notice, it did not have to pay him for the equivalent period as part of the damages based on the period of reasonable notice.

[19] In *Sylvester* v *British Columbia*, [1997] 2 S.C.R. 315, a case dealing with an employee terminated during a period when he was receiving disability benefits, Justice Major stated the following as a general principle of law, at p. 320:

> ...an employee who is wrongfully dismissed without adequate notice of termination is entitled to damages consisting of the salary the employee would have earned had the employee worked during the notice period. The fact that an employee could not have worked during the notice period is irrelevant to the assessment of these damages. They are based on the premise that the employee would have worked during the notice period.

[20] Both parties to this appeal find comfort in the *Rizzo* decision. The Supreme Court of Canada interpreted the *Employment Standards Act* (ESA) of Ontario and determined the rights it gave employees terminated by the bankruptcy of their employer. The liability of an employer to an employee under common law was not in issue. The *ratio* of the case is that an employee who is terminated as a consequence of the bankruptcy of his employer is entitled to the minimal award as provided in the legislation. In the course of arriving at his decision, Justice Iacobucci discussed the policy behind such legislation and used an analogy in which he compared the situation of two employees: one dismissed just before, and one as a consequence of, the bankruptcy. Noble refers to the discussion of policy to support his position that employees' rights are paramount while the KPMG seeks an interpretation of the analogy that would restrict compensation of the employee dismissed before a bankruptcy.

[21] Justice Iacobucci's judgment is replete with policy considerations that support the protection of the interests of employees. He referred to an earlier decision, *Machtinger* v. *HOJ Industries Ltd.,* [1992] 1 S.C.R. 986, where the Court recognized the importance that our society accords to employment and the fundamental role it has assumed in the life of the individual. He noted that, in *Wallace* v. *United Grain Growers Ltd.*, [1997] 3 S.C.R. 701, the Court said that the manner in which employment can be terminated was equally important. He used these principles in giving the ESA a broad interpretation.

[22] His observations about the objective of termination and severance pay apply equally to those terminated at common law. He said one of the primary purposes of notice is to provide employees with an opportunity to take preparatory measures and seek alternate employment. He

characterized termination pay in lieu of notice as a “cushion” for employees against the adverse effects of economic dislocation likely to follow from the absence of an opportunity to search for alternate employment. (Christie, England, Cotter, *Employment Law in Canada* (2nd 3e. 1993) at p. 572-81)

[23] Justice Iacobucci quoted with approval the statements of other courts that severance pay recognizes an employee’s investment in his employer’s business, the extent of which is directly related to years of service and seniority. It follows that long-serving employees suffer special losses when their employment terminates.

The Decision

[24] The chambers judge agreed with the submissions of the KPMG. He held that the bankruptcy limited Noble’s right to common law damages. He found that Noble was entitled to damages for lost wages after the date of the bankruptcy but only for the time period and only in the amount permitted by the *Employment Standards Code*, S.A. 1996, c.E-10.3. As for the period from the date of termination by the employer to the date of the bankruptcy, he found that Noble was entitled to damages for the amount of his base salary plus the bonuses. However, he held that Noble was not entitled to damages for “theoretical sales or profitability which did not occur”.

Analysis

[25] The chambers judge fell into error in two ways. Firstly, he characterized the bankruptcy as an event that reduced the notice period and, using the model of working notice, found it reduced the time Noble might have been employed by Principal. Secondly, he determined that, upon the bankruptcy, the status of Noble changed from that of a person unlawfully terminated by his employer months before, to that of a person terminated by the bankruptcy. He arrived at this determination from a misinterpretation of the analogy used by Justice Iacobucci in *Rizzo.*

[26] The chambers judge accepted the general statement of the law as to the assessment of damages for breach of contract including that an employee must be placed in the same position as he would have been in if the contract had been performed. This statement is the basis for the quantification of damages after a breach. However, the chambers judge accepted KPMG’s argument that it means that the employee should be placed in the same position he would have been in had he worked during the period of notice, which opportunity to work would have been terminated by the bankruptcy. Such an interpretation confuses termination by dismissal and termination by working notice. Since Noble was terminated by dismissal, which was a breach of contract by the employer, he had the right to damages at that date. It is true that, in quantifying those damages, the court should look at the loss from the perspective of the contract having been performed. However, such an analysis does not support shifting the legal position of the

employee who has been unlawfully dismissed without notice to that of a person who has been given working notice. To do so is to err in law.

[27] The chambers judge cited with approval the statements of Justice Lambert in *Dunlop*. In applying them, he found that the bankruptcy was an event that should be considered, and that its effect was to reduce Noble's right to common law damages from the agreed notice period of 18 months to two months. But a close analysis of the statement of Justice Lambert, set out in paragraph 16 of these reasons, does not support this view. The notice period is determinable once and for all at the time of the breach of the employment contract.

[28] Even assuming that the bankruptcy could be considered an event that affected the actual damages suffered by Noble, it is clear that the bankruptcy of Principal not only did not reduce the damages suffered by Noble but also, to the extent that, as an unsecured creditor, his recovery will be less than the full amount awarded, it exacerbated them. The "cushion" will be smaller and therefore the means to recuperate from a dislocation will be less. This case is not similar to those reviewed by the chambers judge where damages actually suffered were reduced by the subsequent event of the payment of benefits or death. Thus, the chambers judge erred in characterizing the bankruptcy in this case as an event that could reduce the period of notice and, even if looked at through the perspective of the effect it had on Noble's damages, it provides no basis to reduce them.

[29] The chambers judge was correct when, in commenting on the *Rizzo* case, he said, at paragraph 27 of his memorandum of judgment;

> The decision of the Supreme Court of Canada in *Rizzo* was that liability for the wage claims of the employees existed under the *Employment Standards Act*, R.S.O. 1980, c.137. No liability was attributed under the common law either by the Ontario Court of Appeal or the Supreme Court of Canada.

[30] But he erred when he went on to conclude:

> The decision therefore provides support for the argument of the trustee that liability for the losses of Mr. Noble at common law ceased at the date of bankruptcy.

[31] The chambers judge arrived at that conclusion because of a misinterpretation of comments by Justice Iacobucci about consistent treatment of employees. The chambers judge concluded that the claims of all dismissed employees, even those with common law rights, must be restricted to that available under the ESA.

[32] Justice Iacobucci said, at paragraph 28:

> ...if the ESA termination and severance pay provisions do not apply in circumstances of bankruptcy, those employees "fortunate" enough to have been dismissed the day before a bankruptcy would be entitled to such payments, but those terminated on the day the bankruptcy becomes final would not be so entitled.

Justice Iacobucci said such a result would be absurd.

[33] In other words, to require that the dismissal be employer-initiated before the ESA would apply would be unfair. The statement cannot be tortured to say that an employee who might have a common law claim, having been dismissed before the bankruptcy by the employer, loses it because of the bankruptcy. It does say that such an employee would be entitled to make a claim under the ESA.

[34] Concluding comments by Justice Iacobucci, at paragraph 41 are helpful.

> In my view, the impetus behind the termination of employment has no bearing upon the ability of the dismissed employee to cope with the sudden economic dislocation caused by the unemployment. As all dismissed employees are equally in need of the protections provided by the ESA, any distinction between employees whose termination resulted from the bankruptcy of their employer and those who have been terminated for some other reason would be arbitrary and inequitable.

[35] This statement was not meant to limit the quantification of the claim of an employee with entitlement to common law damages because of a prior breach of the employment contract but to establish the entitlement of the employee, whose employment contract was breached by the event of the bankruptcy, to ESA benefits. It would be a strange result indeed if Justice Iacobucci's decision were used to restrict the protection given to a long-term employee terminated without cause and without notice or compensation.

[36] There can be no argument that the recovery by the employee entitled to common law damages be based on his status as an unsecured creditor in the bankruptcy, while that of the employee entitled to damages because of the event of the bankruptcy be based in the provisions of the ESA.

[37] Thus, the chambers judge erred in law in finding that Noble's entitlement to common law damages was limited by the bankruptcy. The appeal must be allowed so that Noble is entitled to make a claim for damages based on 18 months' notice.

Damages

[38] Damages were acknowledged to be the equivalent of 18 months' salary, which had two components: a base amount of $5,000 per month and bonuses based on increased sales. There is an issue as to whether Noble is entitled to the bonus monies. KPMG argues that he is not because the increases upon which they would have been based never occurred. The chambers judge found that no damages could be claimed with respect to what he called "theoretical sales or profitability".

[39] The evidence before the court was limited to an agreed statement of facts and an affidavit of the trustee. The following facts emerge from those sources. Noble agreed to compensation that had two parts: one certain, the base salary, and one to be determined, the bonuses. These terms were in an employment contract of June of 1986, approximately 14 months before the termination. By that time, Noble had been employed by Principal for 17 years and was a Senior Vice-President of Finance for the prairie region. Noble himself sold securities and investments to the public and supervised others' doing so.

[40] One bonus was calculated on the basis of increased monthly sales compared to those of the previous year. The other was based on new salespersons reaching certain quotas. Although the term "bonus" was used to describe the payment Noble would receive flowing from all sales, in reality it was payment for incentive-based performance.

[41] Applying the basic principles of law set out earlier, Noble is entitled to compensation for lost bonus monies that were part of his income and therefore, upon his unlawful dismissal, became damages to which he was entitled based on the premise that he would have received them had the contract been performed. The probability is that, during the notice period, had the contract been performed, the incentive compensation would have been earned. In the absence of evidence to the contrary, it is an implied term of the employment contract that an employer will carry on its business in its normal course. In this case, the parties have agreed on the quantum of damages for the bonus component of Noble's salary for the notice period being: 18 x $7261.62 = $129,899.16. There is no evidence as to the basis for the monthly bonus amount used in that calculation. It must be assumed that it was based on sales records prior to the bankruptcy.

[42] Case law cited by the parties indicates that some courts have approved of using past performance in the calculation of bonuses and have awarded bonuses even where the fortunes of the employer company have diminished. *Rosscup* v. *Westfair Foods Ltd.*, [1999] A.J. No. 944 (Alta. Q.B.); *Beach* v. *Ikon Office Solutions Inc.*, [1999] B.C.J. No. 1574 (S.C.); see also, England, Christie and Christie, *Employment Law in Canada* (3rd Ed., Toronto: Butterworths, 1999) at 16.27.

[43] Returning to the judgment of Justice Iacobucci in *Rizzo*, it is important to remember that the objective of termination pay is to provide a "cushion" against dislocation and to recognize the special losses suffered by long-term employees.

[44] It is agreed that in 1988 Noble commenced his own business and earned a net income of $11,658.61 and that in 1989 his net income from the business was $42,429.98. The parties agree that those figures must be taken into account in the final calculations as mitigation of the loss. It would appear that Noble's experience and ability permitted him to shoulder the responsibility of mitigating his loss in a fairly timely and effective manner.

Conclusion

[45] The appeal is allowed. Noble is entitled to damages for breach of contract equivalent to 18 months' notice to include base salary and bonus payments. The parties have agreed that these amounts are $90,000 and $129,899.16, respectively. Appropriate adjustments are to be made for the unpaid wages and mitigation of loss. The parties advise they have agreed on interest. The final figure arrived at after the necessary adjustments is a valid claim in the bankruptcy of Principal.

APPEAL HEARD ON JANUARY 14, 2000

REASONS FILED at CALGARY, Alberta,
this 10th day of May, 2000

_____
PICARD J.A.

I concur: _____
WITTMANN J.A.

REASONS FOR JUDGMENT OF
THE HONOURABLE MR. JUSTICE BERGER

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[46] I have had the advantage of reading in draft form the Reasons for Judgment of my colleague, Picard, J.A. The first and rather narrow issue in this appeal is whether the bankruptcy of an employer deprives an earlier dismissed employee of the damages to which he or she would otherwise be entitled for wrongful dismissal. While I agree with the conclusion reached by my colleague on that issue, I approach the matter in a somewhat different fashion.

[47] The second issue pertains to the Appellant's claim that he is entitled to damages that include a "bonus". In that regard, I respectfully disagree with the opinion of the majority.

[48] The legal analysis is premised on facts that are not in dispute. They are adequately set out in the Reasons for Judgment of my colleague and need not be repeated.

[49] The nature of the implied term in a contract of employment informs the issues at bar. The implied term compels each party to give reasonable notice of termination to the other. Payment of salary or wages in lieu of notice is not an implied term. ***Dunlop v. British Columbia Hydro and Power Authority*** [1988] B.C.J. No. 1963 (B.C.C.A.).

[50] A breach of the implied term occurs on the day of summary termination. The failure to provide notice, in other words, is a breach of the employment contract entitling the employee to damages. The question to be decided is whether those damages crystalize on the day of termination such that an assessment of those damages made after bankruptcy is not affected by that bankruptcy.

[51] What then is the significance, if any, of events following summary dismissal? Damages are derived from a determination of the proper notice period. The proper notice period is determinable once and for all at the time of the breach of contract and is not, itself, affected by subsequent events. ***Dunlop v. British Columbia Hydro and Power Authority***, ***supra***, (at para 17).

[52] That having being said, it is vital to distinguish between the determination of the notice period and the assessment of damages actually suffered by the dismissed employee. I respectfully agree with the following statement of Lambert, J.A. in ***Dunlop*** (at para. 17):

> "I add that, in considering the significant of events following the dismissal, the proper principle, in my opinion, is that an event which occurs after a wrongful dismissal and before trial, or before

> the end of the notice period, whichever comes first, may be considered in assessing the damages actually suffered by the dismissed employee. The legal significance to be attached to the event will depend on the nature of the event and on the other relevant factors in the case."

[53] It follows that in ***Dunlop***, the Court was of the view that the employer could not avail itself of the disability of its employee which arose after the contract had been broken. Breach of contract made that event "inconsequential". As Lambert, J.A. put it "When *B.C. Hydro* broke the contract of employment it lost its right to rely on the provision in that contract that no salary would be paid with respect to a period of disability."

[54] This is precisely the interpretation of ***Dunlop***, ***supra***, given by other courts. By way of illustration, McKeown, J. in ***Card Estate v. John A. Robertson Mechanical Contractors (1985) Ltd***., [1989] O.J. No. 1129 S.C. Ont. - High Court of Justice said this:

> "The sole issue before the B.C. Court of Appeal was whether actual events which occurred after the dismissal and would have prevented the employee from earning income had he served out the notice period would prevent him from being compensated for his wrongful dismissal. The court held that **events which might have occurred had the employer given reasonable notice**, but which hadn't actually happened, could not determine the quantum of damage arising from the dismissal. The employer was not entitled to raise hypothetical alternatives which might have arisen but for its breach of contract."
>
> [Emphasis added]

See also ***Woodlock v. Novacorp International Consulting Inc***., [1990] 6 W.W.R. 454, 72 D.L.R. (4th) 347 (B.C.C.A.), ***McGarry v. Bosco Homes Edmonton***, [1992] A.J. No. 1202.

[55] The Respondent argues that the Supreme Court of Canada's decision in ***Rizzo v. Rizzo Shoes Ltd. (Re)***, [1998] 1 S.C.R. 27, [1998] S.C.J. No. 2 places employees terminated before bankruptcy in the same position as those "terminated" by the act of bankruptcy. The Respondent submits that in ***Rizzo***, the Court was motivated by the unfairness that would result if employees whose termination resulted from a bankruptcy were treated differently than those whose employment had been terminated for some other reason. The Respondent says that the corollary must also be the case. Counsel for the Respondent argues that it would be equally "arbitrary and inequitable", to use the words of Iacobucci, J. at para. 41 of ***Rizzo,*** to give the Appellant a much larger claim in the bankruptcy than those employees who are terminated as a result of the bankruptcy simply because the Appellant's termination occurred a short time prior to the bankruptcy.

[56] I do not read ***Rizzo*** in quite that way. The issue there was entitlement to statutory benefits under the ***Employment Standards Act***. In my view, the case is authority for the proposition that "**any** distinction" that would deprive some employees of **minimum protections** will not be countenanced. That is not the situation in the case at bar. Giving the Appellant his full common law damages will not deprive other employees of their minimum protections under the ***Employment Standards Act***. The Appellant, it is true, will fare better than other employees who remained employed to the date of bankruptcy. But that is precisely what the legal framework contemplates. The principle that emerges from ***Rizzo*** is not that all employees will be treated alike. It is only authority for the proposition that all employees must be accorded their minimum statutory protections. It follows that the Appellant is entitled to 18 months salary in lieu of notice of termination having regard to the length of employment and other factors recited in the agreed statement of facts.

[57] As to the Appellant's claim for a "bonus", reference must first be made to the contract of employment. For purposes of analysis, but without deciding the point, I am prepared to assume that the bonus awarded in prior years forms an integral part of the Appellant's salary.

[58] In the case at bar, the employment contract (as evidenced by letter dated June 12, 1986) sets out a formula for calculating the bonus:

> "Bonuses will be based upon sales improvements within your [the Appellant's] Region:
>
> > a) You will receive $36 for each percentage point increase per month, this month's 3MMA sales volume over last year this month's 3MMA sales volume.
> >
> > i.e. July 1986 3MMA volume in the Prairie region is $15,000,000.
> > July 1985 3MMA volume in the Prairie region is $10,000,000.
> >
> > $15,000,000/10,000,000 equals a 50% increase in volume;
> > therefore, 50 x $36 = $1,800 would be the bonus for July 1986.
> >
> > b) You will receive $500 for each new salesman, in your region, that reaches the qualified consultant status of 500 QPR career volume during the first year of employment."

[59] At the time of this letter agreement, the Appellant had been employed with Principal Consultants Ltd. for a period in excess of 17 years. The record makes clear that the Appellant knew his employer and its business very well. He must be taken to have appreciated that the sales of securities and investments to the public was a business with some considerable risk to it.

Fortunes are made and lost in that financial world. The Appellant's fortunes were tied to his performance, the performance of the sales people under his supervision, and that of the company. He knew full well that the marketplace and its exigencies would play an important role.

[60] Accordingly, it makes sense that the formula for the calculation of bonus would be based on the sales and performance of the company on a monthly basis. On the facts of this case, if that formula were used, the Appellant would receive a bonus for the months following his termination but prior to the assignment in bankruptcy (assuming there was an increase in sales for that period). For the period following bankruptcy, the Appellant would not receive any bonus as the company ceased to have any sales.

[61] Ellen Mole in her text, *Wrongful Dismissal Practice Manual*, Loose Leaf ed. (Butterworths: Vancouver, 1999), says this (at 9.81):

> "Where a bonus during the notice period was unlikely or nonexistent due to the employer's lack of profits, financial situation or general business conditions, no damages will be awarded unless the bonus has been 'guaranteed' or otherwise made part of the employee's basic compensation. Similarly, the fact that the employer did well financially, leading to higher bonuses for other employees, has been considered in assessing damages."

[62] The learned author refers to a number of authorities including ***Weldon v. Com Cor Chemical Ltd.*** (1993), T.L.W. 1244-021 (B.C.S.C.), where payment of bonus was dependent on profits and there was no evidence of profits; ***Ashdown v. Jumbo Video Inc***. (1993), R.L.W. 1309-010 (Ont. Gen. Div.), where bonus payment was dependent on the company receiving its target and there was no evidence that it did; ***Ryshpan v. Burns Fry Ltd.*** (1995), 10 C.C.E.L. (2d) 235 (Ont. Gen. Div.), aff'd 20 C.C.E.L. (2d) 104 (Ont. C.A.), where the court considered the employer's improved financial situation in assessing the amount of the bonus; and ***Knox v. Interprovincial Engineering Ltd***. (1993), 120 N.S.R. (2d) 288, where the evidence established that bonuses related to the financial success of the company and the court award was so premised. In an earlier Alberta decision, ***Stadler v. Terrace Corp. (Construction) Ltd. et al.*** (1983), 41 A.R. 587 (Q.B.), the employee was denied a bonus where there was a provision for a bonus if the hotel or Lake Eden Resort realized a profit and there was no evidence that either did.

[63] The Appellant cites yet another principle in support of the claim for a bonus. On the authority of ***Sylvester v. British Columbia***, [1997] 2 S.C.R. 315, he argues that damages should be awarded on the basis that the employee would have worked during the notice period. In particular, reference is made to the comments of Major, J. in ***Sylvester*** at para. 9:

> "**The fact that an employee could not have worked during the notice period is irrelevant to the assessment of these damages.**

> **They are based on the premise that the employee would have worked during the notice period**. Therefore, an employee who is wrongfully dismissed while working and an employee who is wrongfully dismissed while receiving disability benefits are both **entitled** to damages consisting of the salary the employee would have earned had the employee worked during the notice period."
>
> [Emphasis added]

[64] This passage would, at first blush, tend to support the proposition that a court should not look to events following the date of breach to assess the damages. It will be remembered, however, that in ***Sylvester*** the Court looked to post-breach events to quantify the damages. The issue on appeal was whether the disability benefits received by the Respondent during the notice period should be deducted from the salary he would have earned during the notice period. Major, J. held that the question of deductibility turns on the terms of the employment contract and the intention of the parties. He found that based on the employment contract, the payments were deductible as the parties did not intend the employee to receive both disability payments and damages. It follows that Major J.'s statement in ***Sylvester*** regarding "assessment of damages" refers, in fact, to the employee's **entitlement** to damages, rather than the **quantification** of damages.

[65] The same contract-based approach to **quantify** damages must be used in the case at bar. The relevant inquiry is: what did the parties intend in respect of the bonus payment?

[66] In my view, a plain reading of the contract makes clear that the parties intended a bonus to be paid only where there was an actual increase of sales by the company. This would make sense. Suppose the employer had managed to stay afloat for another 18 months, but earned no profits. Had that occurred, the formula agreed upon would not have generated a bonus for the Appellant.

[67] This approach is consistent with the principle that an employee who is wrongfully dismissed without adequate notice of termination is **entitled** to damages consisting of the salary that the employee would have earned had the employee worked during the notice period. In the case at bar, had the Appellant worked during that period, he would not have received a bonus for the period following bankruptcy. To ignore the bankruptcy and to award a bonus is to place the Appellant in a better situation than if the company had not gone bankrupt but had made no sales. This Court ought not to re-write the contractual arrangement between the parties to achieve such a result.

[68] For these reasons, I would allow the appeal and award the Appellant damages in lieu of notice premised upon 18 months salary together with a bonus for the period following dismissal, but prior to bankruptcy, to be calculated in accordance with the letter agreement of June 12, 1986.

[69] This judgment is styled "Reasons for Judgment Reserved". The label "Reserved" no longer has the significance it once had. The Court's policy set out in ***Hutterian Brethren Church of Starland v. Starland No. 47 (Municipal District)***, (1993) 9 Alta.L.R. (3d) 1, at 15 and ***R. v. Bonneteau*** (1995), 24 Alta.L.R. (3d) 153, at 158 was abolished on September 1, 1999.

[70] The effect of the new policy, which still permits circulation of draft reasons to members of the Court off the panel (for comment only), was stated as follows by Hetherington, J.A. in ***R. v. Fash*** [1999] A.J. No. 1086:

> "In the past this court has said that, so far as statements of law or principle are concerned, a reserved judgment which is not a dissenting judgment sets out views accepted by a majority of the members of the court. (See *Hutterian Brethren Church of Starland v. Starland No. 47 (Municipal District)* (1993), 9 Alta. L.R. (3d) 1, at 15, and *R. v. Bonneteau* (1994), 24 Alta. L.R. (3d) 153, at 158.) However, this is no longer the case. The practices of the court have changed. Now so far as statements of law or principle are concerned, a reserved judgment which is not a dissenting judgment sets out the views of a majority of the panel which heard the appeal. It can not be inferred that a majority of the members of the court share those views."

APPEAL HEARD on JANUARY 14, 2000

REASONS FILED at CALGARY, Alberta,
this 10th day of MAY, 2000

_____

BERGER, J.A.

TAB 10

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *All Canadian Investment Corporation (Re),* 2019 BCSC 1488

Date: 20190904
Docket: S1710393
Registry: Vancouver

In the Matter of the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended

And

In the Matter of the *Business Corporations Act*, S.B.C., c. 57, 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 a Plan of Compromise and Arrangement of All Canadian Investment Corporation

Before: The Honourable Mr. Justice Walker

Reasons for Judgment

Counsel for the Petitioner:	J. West
Counsel for the Redeeming Shareholders:	J. Whyte
Counsel for the Non-Redeeming Shareholders:	M. Davies
Counsel for the creditors, James Hancock and 1083163 Alberta Ltd.:	V. Tickle
Counsel for the Monitor:	D.B. Hyndeman
Place and Dates of Hearing:	Vancouver, B.C. June 18-20, 2019
Place and Date of Judgment:	Vancouver, B.C. September 4, 2019

Table of Contents

Introduction

[1] The petitioner in this insolvency proceeding, All Canadian Investment Corporation ("ACIC"), seeks to determine competing priority claims amongst its preferred shareholders. Its application is brought under the statute governing this proceeding, the *Companies Creditors' Arrangement Act*, R.S.C. 1985, c. C-36 [*CCAA*].

[2] ACIC is incorporated pursuant to the *Business Corporations Act*, S.B.C. 2002, c. 57 [*BCA*].

[3] Prior to its insolvency, ACIC carried on business as a registered mortgage investment corporation ("MIC") since 1998. Its business was to loan funds to third party owners of commercial and residential property, mostly to be secured by mortgages, from a pool of funds it received from time to time from individuals and corporations who invested in ACIC by purchasing preferred shares.

[4] Some of ACIC's preferred shareholders delivered redemption notices to the company prior to the commencement of this proceeding in an effort to be paid an amount equal in value to their original share subscription price. Some, but not all of them, are before the Court on this application. I refer to those who are as the "redeeming preferred shareholders", claim to be creditors of ACIC. They assert that all of ACIC's other shareholders, both preferred and common, rank lower in priority since they are equity claimants.

[5] For ease of identification, I collectively refer to to the preferred shareholders who did not deliver redemption notices or did not deliver them prior to the commencement of this proceeding, as the "non-redeeming preferred shareholders".

[6] The core issue on this application is whether the redeeming preferred shareholders are creditors of ACIC as opposed to equity claimants, so as to share rateably in the distribution of proceeds paid under any court-approved plan of arrangement with the company's other creditors, and in priority to the non-redeeming preferred shareholders and ACIC's common shareholders.

[7] The redeeming preferred shareholders' claim is opposed by ACIC, two of its creditors, and the non-redeeming preferred shareholders. The common shareholders did not appear on the application.

[8] ACIC agreed to take the lead in seeking a determination of the priority issue and brought this application seeking declaratory relief.

[9] The priority claim advanced by the redeeming preferred shareholders must be determined before a suitable plan of arrangement, which would include a claims process and plan for distribution of ACIC's assets, can be submitted for court approval.

[10] It will serve no purpose in these reasons to comment on the length of time it has taken to get to this point in the proceeding. It will suffice to say that at this juncture, all stakeholders are anxious to have a plan presented to the court for approval in this liquidating *CCAA*.

[11] The facts set out in these reasons are my findings of fact.

Positions of the Parties

[12] The redeeming preferred shareholders' position on this application is that they were never equity investors. They assert that when the nature of ACIC's business as a MIC is considered, they are properly characterized as lenders from the outset who are debt claimants because their funds were pooled by ACIC and then loaned out to borrowers. They argue that their individual redemption requests should be viewed as akin to demands on a promissory note. In their submissions, they distinguish themselves from the non-redeeming preferred shareholders on the basis of the redemption notices they delivered to ACIC prior to the commencement of this *CCAA* proceeding.

[13] They also advance an alternative position if they are characterized as equity investors when they purchased their preferred shares. They submit that they later became creditors of ACIC. They rely on what they characterize as the purported contractual effect of various communications from ACIC, including its promotional

materials, to potential and existing investors, in an attempt to establish that the nature of their relationship with ACIC changed.The redeeming preferred shareholders acknowledge that ACIC's Articles and various offering memoranda concerning potential subscriptions for preferred shares ("Offering Memoranda") clearly state that ACIC's obligation to honour redemption requests from preferred shareholders is wholly discretionary, resting with ACIC's directors, which throughout was only one, Mr. Donald Bergman. However, they maintain that those communications altered their contractual relationship with ACIC so as to provide for contractually enforceable guaranteed redemption rights that ACIC was obliged to honour at specific points in time. As a result, they say that ACIC can no longer rely on the discretionary provisions in the Articles and the Offering Memoranda and that ACIC contractually bound itself to pay those redemptions as debts. In the result, the redeeming preferred shareholders submit that their relationship with ACIC changed to become creditors.

[14] In the further alternative, those redeeming preferred shareholders whose redemption requests were partially paid before this proceeding was commenced submit that if they were equity claimants at the outset and if ACIC's communications do not constitute an enforceable contractual right to redemption sufficient to change their relationship with ACIC, then the status of their particular claims has changed, such that any redemption amounts owing are debts owed by ACIC.

[15] The redeeming preferred shareholders concede that the right of each of them to recover as a debt claimant depends on ACIC's financial circumstances at the time their individual redemption notices were delivered since a redemption right is unenforceable per s. 79(1) of the *BCA*, if it means that redemption would render ACIC insolvent:

> 79 (1) A company must not make a payment or provide any other consideration to redeem any of its shares if there are reasonable grounds for believing that
>
> (a) the company is insolvent, or
>
> (b) making the payment or providing the consideration would render the company insolvent.

[16] Language mirroring s. 79 is found in the Offering Memoranda.

[17] The redeeming preferred shareholders acknowledge that at this juncture it is not known which redemption notices were delivered to ACIC at a time when reasonable grounds did not exist to believe that either ACIC was insolvent at the time of the request or that honouring the request would cause it to become insolvent.

[18] Consequently, the redeeming preferred shareholders submit that if they succeed in their claim to be creditors, a further, highly specific and lengthy factual inquiry, involving Mr. Bergman's knowledge when each redemption notice was delivered to ACIC, will have to be made to determine whether s. 79 of the *BCA* is engaged.

[19] The non-redeeming preferred shareholders disagree that the redeeming preferred shareholders are debt claimants. Their position is that all preferred shareholders are equity claimants from the outset and that nothing has changed to alter their status.

[20] Included within the non-redeeming preferred shareholders' submissions is the argument that mirroring the common law, the *BCA* establishes a presumption of equality amongst all shareholders. Each share of a class of shares (in this case, preferred shares) "must have attached to it the same special rights or restrictions as are attached to every other share": ss. 59(4); see also ss. 59(3), 61. Rights related to a share attach to the share, and not to the shareholder: Gower's *Principles of Modern Company Law*, 4th ed. (London: Stevens and Sons, 1979), at 403; *Bowater Canadian Ltd. v. R.L. Crain Inc.* (1987), 46 D.L.R. (4th) 161 at 16 (Ont. C.A.). The presumption is even stronger, they argue, in a *CCAA* proceeding given the broad and flexible authority conferred on the supervising judge to determine a fair and efficient resolution of competing claims in circumstances where there are insufficient financial resources to meet all of them: *CCAA*, s. 11.

[21] In addition, and relying on *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60 at paras. 13-15 and *Bul River Mineral Corporation (Re)*, 2014 BCSC 1732, at paras. 100-101, the non-redeeming preferred shareholders

submit that if the redeeming preferred shareholders' position is correct, the inquiry called for would be unduly protracted and further delay this *CCAA* proceeding, so as to impede any realistic prospect to achieve the statutory objective of an efficient resolution of competing claims.

[22] The non-redeeming preferred shareholders also say that they will be significantly prejudiced because they will recover little to nothing if the redeeming preferred shareholders' claim to be debt claimants prevails.

[23] Some of ACIC's creditors attended the hearing of the application and opposed the redeeming preferred shareholders' claim as well, since there are insufficient assets to pay them out in full if the latter are treated as debt claimants.

[24] ACIC's position on this application is that regardless of any redemption requests, whether paid or unpaid in whole or in part, all preferred shareholders are equity claimants within the meaning of s. 2(1) of the *CCAA*. ACIC seeks a declaration to that effect plus ancillary relief.

[25] For the reasons that follow, I reject the claim advanced by the redeeming preferred shareholders. I have determined that they, along with all of ACIC's preferred shareholders, are equity claimants.

Background Facts

[26] ACIC's shareholders are divided into two groups: common voting shareholders and preferred shareholders. There are currently outstanding four issued common shares and approximately 37,277 preferred shareholders and 15,647 warrants attached to the preferred shares. The preferred shares are stated to be non-voting, "unless otherwise provided for" (and none was).

[27] ACIC issued preferred shares and attached warrants between 1998 and 2015, all in accordance with its articles in force throughout the material time ("Articles").

[28] Draft subscription agreements for the purchase of preferred shares are contained in the various Offering Memoranda issued by ACIC over the years.

[29] Each preferred shareholder acquired units comprised of one preferred share and one warrant (referred to by ACIC by the singular term, “Unit”) by signing a subscription agreement. I refer to them collectively as “Subscription Agreements”. The subscription price for each Unit was fixed at $1,000. Each warrant granted a preferred shareholder a non-transferable option to acquire additional preferred shares for the same price. The total capital value for all issued Units is approximately $37,277,000.

[30] ACIC’s preferred shares contain numerous rights, including a right of redemption (also known as a right of retraction) to receive a return of the purchase price paid for shares, as well as the right to receive dividends so long as an investing subscriber remains a preferred shareholder.

[31] Preferred shareholders were paid dividends from time to time. Between 2005 and 2014, ACIC issued dividends with annual returns ranging between 6.25% and 8%. The return on dividends reduced in 2015 to approximately 2.5%, and to 1% in 2016. ACIC has not issued dividends since 2016.

[32] The redeeming preferred shareholders advise that the earliest redemption requests in issue on the application date back to 2013.

[33] Approximately 540 of ACIC’s preferred shareholders, comprising 27,587 preferred shares with a capital value of $27,587,000, issued redemption notices to ACIC before this *CCAA* proceeding was commenced. As mentioned, not all of those who did are before the Court on this application.

[34] Some redeeming preferred shareholders requested redemption of all of their shares prior to the commencement of this *CCAA* proceeding, while others only requested partial redemptions. Some of those who delivered redemption notices were paid in full, others only in part, and some were not paid at all.

[35] According to ACIC, preferred shares to the value of $1,380,500 were redeemed and paid out prior to the initial order in this proceeding, issued by Madam

Justice Adair on November 10, 2017, leaving a balance of unsatisfied share redemptions of $26,207,000.

[36] Sadly, many of ACIC's preferred shareholders are elderly individuals who invested most if not all of their life's savings with ACIC.

[37] Due to defaults on loans it made to certain third parties, ACIC was unable to pay all of the redemption notices it received from preferred shareholders. It sought protection under the *CCAA*.

[38] In addition to the claims asserted by the redeeming preferred shareholders, when ACIC commenced this proceeding on November 8, 2017, it faced approximately $1.785 million in secured claims and $3.96 million in unsecured claims.

[39] It is now evident that this proceeding is in effect a liquidating *CCAA* as there is no reasonable prospect that ACIC's business can be saved. Its primary asset is its loans portfolio. ACIC maintains an office in this province in Salmon Arm, with two staff members. It is also evident that at the moment, ACIC's creditors and shareholders are better off under the *CCAA* as opposed to a bankruptcy under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 [*BIA*].

[40] Although ACIC has yet to submit a plan of arrangement, the Monitor has been actively engaged in pursuing loan recoveries and operating ACIC's business as per court appointed powers akin to those of a super monitor. Although the Monitor expects to recover a substantial amount of ACIC's loan portfolio, possibly to a maximum of approximately $37.277 million, the Monitor advises that there will be insufficient funds to pay the amounts owed to ACIC's creditors and to return the capital invested by its preferred shareholders.

Overview: Equity vs. Debt Claimants

[41] In a proposed plan of arrangement or compromise submitted for court approval under the *CCAA*, a debtor company may divide its creditors into different

classes. Equity claimants are treated as a single class, unless otherwise ordered: ss. 22(1), 22.1. They rank behind creditors.

[42] Historically, in insolvency matters debt claimants have taken priority to equity claimants. The reasoning behind this approach was explained by Justice Morawetz (as he then was) in *Sino-Forest Corporation (Re)*, 2012 ONSC 4377 at paras. 23-25, aff'd 2012 ONCA 816:

> 23 … Essentially, shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditor claims are not being paid in full. Simply put, shareholders have no economic interest in an insolvent enterprise… [citations omitted]
>
> 24 The basis for the differentiation flows from the fundamentally different nature of debt and equity investments. Shareholders have unlimited upside potential when purchasing shares. Creditors have no corresponding upside potential… [citations omitted]
>
> 25 As a result, courts subordinated equity claims and denied such claims a vote in plans of arrangement… [citations omitted]

[43] Because of the superior position of debt claimants over equity claimants, it has become necessary for courts to distinguish between the two. The general approach for determining whether a party was a debt or equity claimant was set out in *Canadian Deposit Insurance Corp. v. Canadian Commercial* Bank, [1992] 3 S.C.R. 558 [*CDIC*], which was helpfully summarized by Madam Justice Fitzpatrick in *Bul River* at para. 69:

> … In [*CDIC*], the issue was whether money advanced to the debtor bank was in the nature of a loan or a capital investment for the purpose of determining whether the creditors advancing the funds ranked *pari passu* with other unsecured creditors in a winding-up proceeding. Mr. Justice Iacobucci stated that the approach was to determine the "substance" or "true nature" of the transaction (563, 588). His oft quoted statements are found at 590-91, the relevant principles of which can be summarized as follows:
>
> a) the fact that a transaction contains both debt and equity features does not, in itself, determine its characterization as either debt or equity;
>
> b) the characterization of a transaction under review requires the determination of the intention of the parties;
>
> c) it does not follow that each and every aspect of a "hybrid" debt and equity transaction must be given the exact same weight when addressing a characterization issue; and

> d) a court should not too easily be distracted by aspects of a transaction which are, in reality, only incidental or secondary in nature to the main thrust of the agreement.

[44] The reference to a "hybrid" debt and equity transaction in the above noted excerpt includes preferred shares, which are one form of investment that has proven particularly challenging for courts to categorize. Preferred shares are regarded in the case authorities as hybrid instruments that may contain rights and conditions attributable to both equity and debt: *Royal Bank of Canada v. Central Capital Corp.* [1996] O.J. (3d) No. 359 at para. 127 (C.A.).

[45] The Ontario Court of Appeal said in *Sino-Forest*, at para. 53, that the 2009 amendments to the *CCAA* significantly expanded the definition of equity claims in a manner that "altered" common law. The Court of Appeal determined that the definition extends beyond a holder of an equity interest, and now includes persons that might not otherwise be within its plain meaning (such as advancing claims for contribution or indemnity against the company).

[46] In *Sino-Forest*, shareholders made claims within the *CCAA* proceeding against the company's auditors who in turn sought indemnity from the company. Even though the auditors were never shareholders, their indemnity claim was characterized as an equity claim. I have excerpted what I consider to be guiding language in the Court of Appeal's reasons:

> [1] In 2009, the [*CCAA*] was amended to expressly provide that general creditors are to be paid in full before an equity claim is paid.
>
> [2] This appeal considers the definition of "equity claim" in s. 2(1) of the CCAA. More particularly, the central issue is whether claims by auditors and underwriters against the respondent debtor, Sino-Forest Corporation ("Sino-Forest"), for contribution and indemnity fall within that definition. The claims arise out of proposed shareholder class actions for misrepresentation.
>
> …
>
> [37] We agree with the supervising judge that the definition of equity claim focuses on the nature of the claim, and not the identity of the claimant. In our view, the appellants' claims for contribution and indemnity are clearly equity claims.
>
> …
>
> [39] The definition [of equity claim] incorporates two expansive terms.

> [40] First, Parliament employed the phrase "in respect of" twice in defining equity claim: in the opening portion of the definition, it refers to an equity claim as a "claim that is in respect of an equity interest", and in para. (e) it refers to "contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d)"…
>
> [41] The Supreme Court of Canada has repeatedly held that the words "in respect of" are "of the widest possible scope", conveying some link or connection between two related subjects. …
>
> …
>
> [46] "Equity claim" is not confined by its definition, or by the definition of "claim", to a claim advanced by the holder of an equity interest. Parliament could have, but did not, include language in para. (e) restricting claims for contribution or indemnity to those made by shareholders.
>
> …
>
> [53] In our view, the definition of "equity claim" is sufficiently clear to alter the pre-existing common law…

[47] Taking the same approach as the Court of Appeal and Mr. Justice Morawitz (as he then was) in the court below (at paras. 86-90) in *Sino-Forest*, Fitzpatrick J. noted in *Bul River*, following a most helpful and thorough discussion of case authorities and the relevant 2009 amendments to the *CCAA*, that in one sense, the amendments codified previous case law concerning equity claims, but also provided for a broader yet more concrete definition of equity claims.

[48] Relying on the reasons of Laskin J.A. in *Central Capital*, Fitzpatrick J. also pointed out that in the context of a *CCAA* proceeding, particularly in light of the 2009 amendments, the mere existence of redemption rights does not equate preferred shareholders as creditors:

> [105] In the same manner, the new equity provisions in the *CCAA* reinforce that it remains an important policy objective that equity claims be subordinated to debt claims. In *Sino-Forest Corporation*, the Court of Appeal focused on the purpose of the 2009 amendments and stated:
>
> > [56] In our view, in enacting s. 6(8) of the *CCAA*, Parliament intended that a monetary loss suffered by a shareholder (or other holder of an equity interest) in respect of his or her equity interest not diminish the assets of the debtor available to general creditors in a restructuring. If a shareholder sues auditors and underwriters in respect of his or her loss, in addition to the debtor, and the auditors or underwriters assert claims of contribution or indemnity against the debtor, the assets of the debtor available to general creditors would be

> diminished by the amount of the claims for contribution and indemnity.
>
> [106] This same recognition of the sound policy objectives of insolvency legislation was noted by Laskin J.A. in *Central Capital* (ONCA). He commented at 546 that "[p]ermitting preferred shareholders to be turned into creditors by endowing their shares with retraction rights runs contrary to this policy of creditor protection."
>
> [107] I see no principled basis upon which a different approach should be taken in respect of an equity claimant who has had the foresight, energy or just plain luck to seek and obtain a judgment prior to the filing date.
>
> [Emphasis added.]

[49] Accordingly, while the 2009 amendments did represent in part a codification of the previous case law concerning equity claims, they also represent a more concrete definition of "equity claims" and by such definition a broadening and more expansive definition of such claims: *Sino-Forest* (ONCA) at paras. 24, 34-60. Parliament has now clearly cast the net widely in terms of the broad definition of equity claims such that claims that might previously escaped such characterization will now by caught by the *CCAA*.

CCAA

Introductory Remarks

[50] The provisions of the *CCAA* greatly assist in the analysis. The expanded definition of equity claim and the definition of equity interest clearly suggest that ACIC's preferred shares, which include rights of redemption and to receive dividends, constitute equity interests and provide strong support for the position taken by ACIC and the non-redeeming shareholders that all preferred shareholders in this *CCAA* proceeding must be treated as equity claimants.

[51] An appropriate starting point in the analysis is with a brief discussion of the key provisions and objectives of the *CCAA*, particulary in light of ACIC's submission that the priority issue is easily resolved in favour of its position on the application from the broad definition of "equity clamant" and "equity interest" in the statute without the need for a detailed analysis of the underlying transaction documents.

Statutory Definition of Equity Claim

[52] As a result of the 2009 amendments to the *CCAA*, an "equity claim" is defined in s. 2(1) and includes redemption claims:

> 2(1)
>
> …
>
> **equity claim** means a claim that is in respect of an equity interest, including a claim for, among others,
>
> **(a)** a dividend or similar payment,
>
> **(b)** a return of capital,
>
> **(c)** a redemption or retraction obligation,
>
> **(d)** a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
>
> **(e)** contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d)…
>
> [Emphasis added.]

[53] An "equity interest" is also defined, and includes a share in the company and a warrant to acquire additional shares:

> **2(1) equity interest** means
>
> **(a)** in the case of a company other than an income trust, a share in the company — or a warrant or option or another right to acquire a share in the company — other than one that is derived from a convertible debt, and
>
> **(b)** in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt;

No Statutory Definition of Creditor

[54] Unlike the *BIA*, there is no definition of creditor in the *CCAA*. In the *BIA*, a creditor is defined in s. 2 as "a person having a claim provable as a claim".

[55] The *CCAA* contains a broad definition of "claim" in s. 2, which incorporates the definition in the *BIA*:

> **claim** means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the [*BIA*].

[56] A "provable claim" is defined in s. 2 of the *BIA* as follows:

> **claim provable in bankruptcy, provable claim** or **claim provable** includes any claim or liability provable in proceedings under this Act by a creditor.

[57] Section 121 of the *BIA* speaks to the meaning of a "provable claim". It provides that all debts and liabilities, including those payable at a future date, to which the bankrupt is subject on the date of bankruptcy by reason of an obligation incurred before bankruptcy.

[58] In *Bul River*, Madam Justice Fitzpatrick points out, at para. 39, that the definition of "claim" found in s. 2 of both statutes "represents a point of convergence consistent with the harmonization of certain aspects of insolvency law under both the *CCAA* and *BIA*: *Century Services* at para. 24.

[59] In the past, the claims and rights of shareholders have not been treated as provable claims and ranked behind creditors of an insolvent corporation in liquidation: *Nelson Financial Group Ltd.*, 2010 ONSC 6229 at para. 25. That remains the case under the current *CCAA*. No plan or arrangement may be sanctioned by the court where equity claimants have priority to creditors. Section 6(8) of the *CCAA* states:

> **Compromises to be sanctioned by court**
>
> **6** …
>
> **Payment — equity claims**
>
> **(8)** No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

[60] The rationale is that equity claimants (commonly thought of as investors) are considered to take a higher degree of risk in a company's economic fortunes than creditors who do not share in any upside in the profits or value of the company and the risk of failure.

[61] The following excerpt from *Nelson Financial* aptly describes the distinction between debt and equity claimants:

> [25] … As noted by Laskin J.A. in *Re Central Capital Corporation*, on the insolvency of a company, the claims of creditors have always ranked ahead

> of the claims of the shareholders for the return of their capital. This principle is premised on the notion that shareholders are understood to be higher risk participants who have chosen to tie their investment to the fortunes of the corporation. In contrast, creditors choose a lower level of exposure, the assumption being that they will rank ahead of shareholders in an insolvency. Put differently, amongst other things, equity investors bear the risk relating to the integrity and character of management.

[62] Creditors' claims, including repayment terms and any rates of interest are typically governed by specific, fixed terms: *Bul River* at paras. 65-66; *Nelson Financial* at para. 25; *Sino-Forest* (ONCA) at para. 30.

[63] Although not a *CCAA* case, the Court of Appeal's discussion of the nature of a debt relationship in *Coast Capital Savings Credit Union v. British Columbia (Attorney General)*, 2011 BCCA 20 provides guidance for the issues in this case, particularly in the absence of a statutory definition. At para. 57, Madam Justice Newbury adopted the following definition, which she noted was also found in numerous Canadian and English authorities:

> A debt is defined to be a sum of money which is certainly, and at all events, payable without regard to the fact whether it be payable now or at a future time.

[64] At para. 23, Newbury J.A. also referred to a definition of debt in a case authority cited by the chambers judge in that case - *A. Valin Petroleums Ltd. v. Imperial Oil Ltd.*, 2007 ABQB 134 at paras. 39-40:

> 39 The word "equity" is not ambiguous. It is a word of ordinary use, particularly in the commercial context….
>
> 40 Debt and equity are distinct concepts. Debt is a claim on the assets of the corporation and is created when money is borrowed. With it arises an obligation on the corporation to repay that money. Corporate equity, however, is comprised of the corporation's total assets unencumbered by debt or other liabilities. It is the "residual economic interest in the corporation's assets, after all outstanding debts have been satisfied." See C. Nicholls, *Corporate Finance and Canadian Law* (Toronto: Carswell, 2000 at page 9).
>
> [Emphasis added.]

[65] Similar definitions, drawn from *Black's Law Dictionary*, *Jowitt's Dictionary of the English Language*, and *The Shorter Oxford Dictionary*, are referred to by the

Ontario Court of Appeal in *Central Capital* at 508, which again involved a *CCAA* proceeding.

[66] There is some conflict in the case authorities as to whether a claim can be considered a debt claim where it is unenforceable: see, e.g. *Bul River* at para. 40; *Central Capital* at 531-534. However, I do not need to decide that issue in order to determine the status of the redeeming preferred shareholders' claims.

Further Analysis is Required

[67] As I said at the outset of this section, the *CCAA* provides considerable guidance in determining the claim of the redeeming preferred shareholders. I agree with ACIC that the 2009 amendments show Parliament's intention to broaden the scope of equity claimants to include shareholders with redemption claims.

[68] However, redeemable preferred shares are viewed in the case law to be "somewhat different than conventional equity capital": *Central Capital* at para. 128; *Coast Capital* at para. 49. In *Central Capital,* Mr. Justice Laskin, in his reasons (concurring with Madam Justice Weiler in the majority), described preferred shares as "compromise securities" and "financial mongrels" with rights analogous to rights of creditors:

> 127 Preferred shares have been called "compromise securities" and even "financial mongrels: Grover and Ross, *Materials and Corporate Finance* (1975), at p. 49. Invariably the conditions attaching to preferred shares contain attributes of equity and, at least in an economic sense, attributes of debt. Over the years financiers and corporate lawyers have blurred the distinction between equity and debt by endowing preferred shareholders with rights analogous to the rights of creditors. One example is the right of redemption -- the right of the corporation to compel preferred shareholders to sell their shares back to the corporation. Another example, and it is the case before us, is the right of retraction -- the right of shareholders to compel the corporation to buy back their shares on a specific date for a specific price.
>
> 128 I acknowledge, therefore, that redeemable or retractable preferred shares are somewhat different from conventional equity capital. What makes the appeals before us difficult is that although the appellants appear to hold equity, their right of retraction appears to be a basic characteristic of a debtor-creditor relationship: see Grover and Ross, supra, at pp. 47-49; Buckley, Gillen and Yalden, *Corporations: Principles and Policies*, 3d ed. (1995), at pp. 938-40.

[69] The fact that a hybrid instrument contains elements of both equity and debt is not an obstacle to determining its true nature: *CDIC* at 590. In *Central Capital*, Laskin J.A. described the nature of the inquiry in this way:

> 129 If the certificate or instrument contains features of both equity and debt – in other words if it is hybrid in character - then the court must determine the "substance" of the relationship between the holder of the certificate and the company. …
>
> 130 In determining the substance of the relationship, as in any other case of contract interpretation, the court looks to what the parties intended. In *CDIC v. CCB*, *supra*, Iacobucci J. put this proposition as follows at p. 588:
>
> > As in any case involving contractual interpretation, the characterization issue facing this Court must be decided by determining the intention of the parties to the support agreements. This task, perplexing as it sometimes proves to be, depends primarily on the meaning of the words chosen by the parties to reflect their intention. When the words alone are insufficient to reach a conclusion as to the true nature of the agreement, or when outside support for a particular characterization is required, a consideration of admissible surrounding circumstances may be appropriate.

[70] Consequently, the focus of the inquiry is to determine whether in substance the redeeming preferred shareholders' claims are debt or equity. They cannot be both.

Determining the Substance of the Relationship

Overview

[71] The inquiry focuses on the transaction documents at the time the relationship was created. It is, generally speaking, informed by the words chosen by the parties to reflect their intentions in conjunction with the principles underpinning insolvency legislation, which in this case includes the remedial purposes of the *CCAA*. Where the words are insufficient to determine the true nature of the agreement, admissible evidence of surrounding circumstances may be considered: *CDIC* at 588, 590; *Central Capital* at paras. 38, 67, 126, 129-130, 135-136.

[72] Section 2(1) of the *CCAA* is clear that in the context of a *CCAA* proceeding, a redemption claim is not indicative of a debt relationship. As well, redemption rights on their own do not create a debtor-creditor relationship. They are to be considered, along with risk-taking, profit sharing, and the right to participate in the assets of the company on liquidation after creditors are paid, as "hallmarks" of a shareholder relationship and an equity interest. To establish a debt relationship, either or both the company's articles or the transaction documents must make it clear that a shareholder's redemption is repayment of a loan: *Central Capital* at paras. 70, 97, 135-136; *Bul River* at para. 109; *Dexior Financial Inc. (Re)*, 2011 BCSC 348 at paras. 12-13,16.

[73] As Weiler J.A. explained in *Central Capital*, language consistent with a debt obligation upon redemption must be reflected in the transaction documents:

> 97 Looked at another way, after the retraction date and at the time of the reorganization, the common features of a debtor-creditor relationship are not in evidence in Central Capital's articles. The agreements between the parties contain no express provision that the redemption of the shares is in repayment of a loan. The corporation was not obliged to create any fund or debt instrument to ensure that it could redeem the shares on the retraction date. There is no indemnity in the event that the money is not repaid on the retraction date. There is no provision for the payment of any interest after the retraction date in the event that the money is not repaid on the retraction date. There is no provision that after the retraction date and in the event of insolvency, the appellants would have the right to have the company wound up. (See *R v. Imperial General Properties Ltd.*, [1985] 2 S.C.R. 288, 21 D.L.R (4th) 741, for a case where the articles of the company contained this right.) There is no provision that upon a winding-up or insolvency the parties are entitled to rank pari passu with the creditors as was the case in *Canada Deposit Insurance Corp. v. Canadian Commercial Bank, supra*.

[74] In *Central Capital*, the parties' intention was (according to the two concurring reasons in the majority) reflected "mainly" in the share purchase agreements, conditions attaching to the shares, the company's articles, and the manner in which Central Capital recorded the shares in its financial statements. They did not establish a debt obligation on the part of the company: see, e.g., para. 131.

[75] Incidental or secondary aspects of a transaction, such as mechanisms for enforcement, should not distract the inquiry: *CDIC* at paras. 46-54; *Earthfirst Canada Inc. (Re)*, ABQB at para. 5.

Examples

[76] Useful guidance for the inquiry into the true nature or substance of the relationship between preferred shareholders and ACIC can also be drawn from some of the cases cited by the parties in submissions.

[77] In *Bul River*, Fitzpatrick J. rejected the claim of certain preferred shareholders that their equity claims converted into debt claims simply because they had obtained (default) judgment for their redemptions against one of the insolvent companies: paras. 85-98, 103-117.

[78] In *Return on Innovations Capital Ltd. v. Gandi Innovations Ltd.*, 2011 ONSC 5018, it did not matter that a claim by a shareholder seeking recovery of share purchase proceeds in the amount USD $50 million was founded on breach of contract and fraud. The legal basis for the claim was not the “deciding factor”. Nor were the “legal tools” used by the claimant, because, Mr. Justice Newbould said, at para. 59, they were being used to recover an equity investment.

[79] In *Nelson Financial*, which was a *CCAA* proceeding, Madam Justice Pepall (as she then was) disagreed that the preferred shareholders were debt claimants. In that case, the company raised money by two different means: from lenders to whom it issued promissory notes with an annual rate of return of 12% and from investors to whom it issued non-voting preferred shares with an annual dividend of 10%. The company’s articles provided the company with unilateral redemption rights on payment of the purchase price plus accrued dividends. At least one investor negotiated a right of redemption and two redemption requests were outstanding as of the *CCAA* filing date. The company’s financial statements also treated the shareholders as equity investors and distinguished them from its creditors.

[80] After referring to the distinction between debt and equity claimants, Pepall J. discussed the broad scope ascribed to the meaning of an equity claim or interest:

> [26] This treatment also has been held to encompass fraudulent misrepresentation claims advanced by a shareholder seeking to recover his investment: *Re Blue Range Resource Corp.* In that case, Romaine J. held that the alleged loss derived from and was inextricably intertwined with the shareholder interest. … *National Bank of Canada v. Merit Energy Ltd*. and *Earthfirst Canada Inc.* both treated claims relating to agreements that were collateral to equity claims as equity claims. These cases dealt with separate indemnification agreements and the issuance of flow through shares. The separate agreements and the ensuing claims were treated as part of one integrated transaction in respect of an equity interest. The case law has also recognized the complications and delay that would ensue if *CCAA* proceedings were mired in shareholder claims.

[81] In addition to reviewing the articles of the company and the share certificates, Pepall J. considered the following evidence of surrounding circumstances at para. 31:

(a) investors' right to receive dividends (said to be "a well recognized right of a shareholder");

(b) investors were given the option of investing in promissory notes or preference shares and opted for the latter;

(c) on liquidation, dissolution, or winding up, preferred shareholders ranked ahead of common shareholders; and

(d) shares were treated as equity in the company's financial statements and in its books and records.

[82] In the result, and although she found characteristics of both debt and equity claims in the relationship, she concluded that the substance of the relationship between the preferred shareholders and the company was equity, not debt: paras. 31-32.

[83] In the *CCAA* case of *JED Oil Inc. (Re),* 2010 ABQB 295, the analysis focused on the relationship at the time the shares were issued when considering the true nature of the claims of preferred shareholders for unpaid dividends. Madam Justice Kent rejected the shareholders' claim as creditors of debt claims. There was no language in the share certificates to establish that dividends were declared and

owing on the date the shares were issued. She found that the substance of the relationship at the time the shares were purchased was not creditor-debtor. The shareholders, she said at para. 16, "are risk-takers, not creditors. For them to become creditors from the time they are issued the shares would require more explicit wording than is contained in these shares."

[84] Lastly, in *Dexior Financial*, which involved a *BIA* proceeding, the fact that a redemption notice was issued prior to bankruptcy "does not change the original intention or substance of the claim": para. 16.

Summary

[85] To summarize, courts take into account a number of factors when determining the substance of the relationship when assessing the status of preferred shareholders. Examples include:

(a) The specific language contained in the company's articles and the transaction documents.

(b) The right of a shareholder to redeem their shares. The absence of this right is inconsistent with a creditor relationship. A right of redemption is particularly compelling as an *indicia* of a creditor relationship where the articles or transaction documents expressly provide that the redemption is for the repayment of a loan.

(c) Whether the shareholder had upside potential in the return of their investment, which indicates an equity relationship and also shared in the downside risk of a lower return.

(d) Whether the shareholder had the right to receive dividends, which is a strong *indicia* of an equity relationship.

(e) Treatment on liquidation, dissolution, or winding up.

(f) Whether the shares are treated as equity or debt in the financial statements of the corporation.

[86] The mechanism used to enforce redemption rights is irrelevant. The legal basis for any claim brought to collect on a redemption request is as well.

The Relationship between ACIC and Its Preferred Shareholders

Overview

[87] As mentioned at the outset of these reasons, I reject the redeeming preferred shareholders' claim that they are debt creditors of ACIC. None of ACIC's preferred shareholders are debt claimants. The redeeming preferred shareholders were not lenders *ab initio* as opposed to investors. They are equity claimants and rank together with all other preferred shareholders and are to be treated as such in the same class in this *CCAA* proceeding.

[88] The relationship between ACIC and its preferred shareholders is comprised of the Articles, the various Subscription Agreements, Offering Memoranda, and applicable legislation such as the *BCA*. The inquiry in this particular case is also governed by the *CCAA*. From them those sources, the substance of the relationship between ACIC and its preferred shareholders, including those who have delivered redemption requests, can be readily ascertained.

[89] The Articles, Offering Memoranda, and Subscription Agreements are clear that the relationship between ACIC and its preferred shareholders is an equity relationship. The preferred shareholders are clearly identified as investors who purchased non-voting preferred shares with rights to receive dividends at various rates dependent on ACIC's financial performance and with redemption rights which throughout may or may not be honoured as determined by ACIC's directors in their sole discretion.

[90] There is no language in the Articles suggesting, directly or indirectly, that a share redemption is in respect of a repayment of a debt. There is also no language, direct or indirect, in the Articles suggesting that preferred shareholders are lenders or that their investment is secured by a promissory note or something akin to it. Article 27.1 defines preferred shares as "without par value in the capital of the Company".

[91] Prefered shareholders took the advantages of the potential upside in ACIC's earnings obtained from increasing lending rates as well as the risk of loss of their entire investment.

[92] The risks of the investment are clearly outlined to potential investors. The Offering Memoranda characterized the "investment" as both "risky" and "speculative". Each Offering Memoranda contains a detailed discussion (including warnings) of numerous risk factors associated with an investment with ACIC, including its speculative nature, the absence of a market to transfer or assign shares and warrants, and no guarantee that dividends would be declared or paid. The Offering Memoranda also advise that their contents had not been reviewed by any regulatory authority.

[93] The Offering Memoranda also describe the purchase of preferred shares as a speculative risk that should be considered only by subscribers who are able to withstand the loss of their total investment:

> ***Item 8 Risk Factors***
>
> The purchase of Units involves a number of significant risk factors. **Any or all of these risks, or other as yet unidentified risks, may have a material adverse effect on the Company's business, the value of the Preferred Shares and/or the return to Preferred Shareholders.**
>
> (a) **Investment Risk**
>
> **(i) Speculative Nature of Investment**
>
> **This is a speculative offering. The purchase of Units involves a number of significant risk factors and is suitable only for Subscribers who are aware of the risks inherent in mortgage investments and the real estate industry and who have the ability and willingness to accept the risk of the total loss of their invested capital and who have no immediate need for liquidity.**
>
> [All emphasis in original.]

[94] In some of the Offering Memoranda, ACIC's capital structure is described and shown to be comprised of common and preferred shares and is specifically distinguished from debt.

[95] The Subscription Agreements also contain language making it clear that each subscriber for preferred shares is making an investment, e.g.:

> **2. REPRESENTATIONS, ACKNOWLEDGMENTS AND CONVENANTS**
>
> 2.1. The Subscriber acknowledges represents and covenants that:
>
> …
>
> (j) the Subscriber is purchasing the Units as principal for investment only and not with the view to the resale or distribution thereof;
>
> [Bold in original]

[96] A subscriber for preferred shares is required to sign a Form 20A per the *Securities Act*, R.S.B.C. 1996 c. 418 confirming, *inter alia*:

> 4. I acknowledge that:
>
> …
>
> (c) I may lose all of my investment; …

[97] There is no language in the Subscription Agreements suggesting that a subscriber for preferred shares is a lender or creditor through any other capacity.

[98] I disagree with the redeeming preferred shareholders' submission that a key *indicia* of an equity investor is defined in part by the word "unlimited" in respect of the opportunity to participate in the financial upside of the company if "unlimited" signifies there can be no possible limit on the rate of return.

[99] They rely on a reading of the reasons in *Sino-Forest* (ONSC) at para. 30 and argue that given the exigencies of the mortgage lending market, it was never possible for them to participate in an "unlimited financial upside" of ACIC. They point to what they characterize as a cap on their highest rate of return for dividends and say that in effect, their relationship with ACIC was akin to creditor and debtor.

[100] In my opinion, "unlimited upside" refers to the possibility of enjoying the benefits of ongoing and potentially increasing profits of the company.

[101] For ACIC, the rates of return, and hence its revenues and profits, depended on market conditions and were not fixed to any maximum. Preferred shareholders always retained the opportunity to share in higher rates of return if market conditions changed to allow for higher lending rates. Conversely, they also took the risk of lower rates of return resulting from potential adverse market conditions and

impediments to ACIC's ability to collect on its loan portfolio (both of which have occurred). I agree with the submission of the creditors who appeared on the application that the investment made by the preferred shareholders is akin to an investment in a fluctuating commodity.

[102] I also disagree with the redeeming preferred shareholders that the fact that ACIC pooled investors' funds indicates a debt relationship or establishes the preferred shareholders as lenders. Pooling from investors is the means by which a MIC such as ACIC is able to carry on business to lend funds to third party borrowers.

[103] I will conclude this section with this observation. If the redeeming preferred shareholders' position that the nature of their relationship from the outset is one of creditor is correct, then it would defeat their claim to be contrasted from the non-redeeming preferred shareholders since all of ACIC's preferred shareholders would be debt as opposed to equity claimants and rank alongside ACIC's other creditors.

Redemption Rights Do Not Affect the Outcome

[104] The redeeming preferred shareholders place significant reliance on their redemption rights (to seek the return of their principal investment amount) as *indicia* of a debt relationship.

[105] In this case, when considered in context, the mere presence of redemption rights do not establish a debt relationship. The intention of ACIC and the preferred shareholders expressed in the Articles and the transaction documents does not establish a debt relationship. There is no language in the Articles, the various Offering Memoranda, and the Subscription Agreements that indicates that the redemption is in repayment of a debt. Furthermore, preferred shareholders were advised throughout that their redemption rights were not guaranteed.

[106] The redemption provisions do not state or suggest that subscribers for preferred shares are lenders. Nor do they state or suggest that preferred shares are given as security akin to a promissory note. Unlike a promissory note, which typically contains a promise to pay by a certain date or the happening of a certain event(s), ACIC's obligation to honour redemption requests was always in the sole discretion of

its directors, who may also clarify or establish terms and conditions for redemption should they consent to a request.

[107] The *BCA* requires that all rights attached to shares be set out in a company's articles: ss. 11(h), 12(2)(b), 48. The Articles state that redemption is in the sole discretion of ACIC's directors. As noted in the previous section, the redemption provisions in the Articles are found in article 27.4. According to Mr. Bergman, ACIC's sole director throughout, ACIC's redemption policy remained unchanged since it began issuing preferred shares in 1998.

[108] Article 27.4 specifically deals with redemption requests from preferred shareholders. Mr. Bergman's sole discretion to consent to or reject redemption requests is clear:

> **27.4 Redemption of Preferred Shares**
>
> A Preferred Share will be redeemed by the Company if and only if:
>
> (a) the Company has received written notice from the registered holder of the Preferred Share that he wishes the Company to redeem the Preferred Share;
>
> (b) the Directors, in their sole discretion, consent to the redemption by the Company of the Preferred Share pursuant to terms and conditions set by the Directors in their sole discretion; and
>
> (c) the Preferred Shareholder who requested that his Preferred Share be redeemed, accepts the terms and conditions of redemption set by the Directors.
>
> The Directors will not be obligated to provide any reasons for not consenting to a Preferred Shareholder's request to have his Preferred Shares redeemed by the Company.
>
> [Bold in original.]

[109] Further, and in contrast to *Nelson Financial*, there are no provisions in the Articles or transaction documents obliging ACIC to buy back shares. To the contrary, Article 8.2 provides that if ACIC proposes at its option to redeem some but not all of the shares of any class or series, then it is in the discretion of its directors subject to special rights and restrictions attached to each share. ACIC's directors are given the discretion whether to decide the manner in which the shares to be redeemed are selected and whether the redemption is *pro rata*.

[110] Turning to the Offering Memoranda, those documents contain detailed information concerning the redemption process and restrictions on redemption requests. Mr. Bergman's discretion to consent or refuse to honour redemption requests is a pervasive theme in the various Offering Memoranda.

[111] For example, ACIC's first Offering Memoranda issued in 1998 warns potential subscribers that redemptions are not guaranteed and may never be honoured:

> **Redemption of Preferred Shares:** The Director of the Company has adopted a Policy regarding the redemption of Preferred Shares. A copy of such policy is available from the Company upon request.
>
> **Pursuant to such policy, a Preferred Share will be redeemable by the Company in certain circumstances. Although the Company will use its best commercial efforts to ensure that all requestsfor redemption are fulfilled, depending on such circumstances the Company cannot guarantee that any or all of the Preferred Shares in respect of which requests for redemption are received will be redeemed in any fiscal year. See Item 8 – "Risk Factors" – Limited Redemption Rights**.
>
> …
>
> The Company will no redeem any Preferred Shares if at the time of such redemption the Company is insolvent or if such redemption will render the Company insolvent, if such redemption will reduce the Company's cash reserves below a level which the Directors determine, in their sole discretion, to be prudent, or if such redemption will cause the Company to breach the requirement that at least 50% of the cost amount of its property must consist of bank deposits or mortgage loans made in respect of residential properties.
>
> [All emphasis in original.]

[112] In addition to the the sole discretion to honour a redemption request vesting with the director, the Offering Memoranda spell out other limitations on redemptions, e.g., adverse financial circumstances including liquidity issues:

> **No Guaranteed Dividends**
>
> The dividends in which the Preferred Shareholders are entitled to participate are **not** cumulative and will not be paid unless such dividends have been declared by the Directors. The Directors have the sole discretion as to whether or not any such dividends are declared. Therefore, there is no guarantee that dividends payable to Preferred Shareholders will be declared.
>
> [All emphasis in original.]

[113] The Offering Memoranda issued in 2001 and 2002 provide another example. They are clear that redemption depends on the consent of the directors in their "sole

discretion" pursuant to "terms and conditions set by the Directors". Subscribers are advised that the "Directors will not be obliged to provide any reasons for not consenting to a Preferred Shareholders' request to have their Preferred Shares redeemed by the Company".

[114] Commencing in 2003, the Offering Memoranda referred to a redemption policy and included a summary making it clear that redemption remained in the discretion of its directors to amend or cancel it, adopt an alternative policy, or refuse to consent to a redemption.

[115] This example is taken from the 2003-2006 and 2015 Offering Memoranda:

> **Redemption of Preferred Shares**: The Company has adopted a policy regarding the redemption of Preferred Shares. A copy of such policy is available from the Company upon request.
>
> **Pursuant to such policy, a Preferred Shareholder will be redeemable by the Company in certain circumstances. Although the Company will use its best commercial efforts to ensure that all requests for redemption are fulfilled, depending on such circumstances the Company cannot guarantee that any or all of the Preferred Shares in respect of which requests for redemption are received will be redeemed in any given fiscal year**. …
>
> …
>
> The Company will not redeem any Preferred Shares if at the time of such redemption the Company is insolvent or if such redemption will render the Company insolvent, if such redemption will reduce the Company's cash reserves below a level which the Company's directors (the "**Directors**") determine, in their sole discretion, to be prudent, or if such redemption will cause the Company to breach the requirement that at least 50% of the cost amount of its property must consist of bank deposits or mortgage loans made in respect of residential properties.
>
> Further, in any calendar quarter, the Company will not redeem any more than that number of Preferred Shares which is equal to 2 1/2 % of the outstanding Preferred Shares at the end of the immediately preceding calendar quarter. ...
>
> …
>
> **The adoption of its policy regarding the redemption of Preferred Shares does not fetter the discretion of the Directors of the Company from time to time to amend or cancel such policy in whole or in part or to adopt an alternative policy with respect to the redemption of Preferred shares, or to refuse to consent to a Requesting Shareholder's request to have their Preferred Shares redeemed by the Company.**
>
> [All emphasis in original.]

[116] Nothing in ACIC's redemption policies removed or otherwise constrained Mr. Bergman's unfettered discretion to consent or refuse to honour redemption requests.

[117] The redemption policy that ACIC adopted (in accordance with s. 27.4 of the Articles) on December 1, 2006 serves as a useful example of its ongoing retention of discretion to honour redemption requests. The policy language is clear that ACIC's new policy did not fetter the discretion of its director from time to time to amend or cancel it in whole or in part or refuse to consent to a redemption request:

> B. Pursuant to Section 27.4 of the Articles of the Company, Preferred Shares are redeemable by the holder provided that:
>
> …
>
> 2. The Company's Director, in his sole discretion consents to such redemption pursuant to terms and conditions set by the Director in his sole discretion; and
>
> 3. The holder accepts the terms and conditions of redemption set by the Director.
>
> The Director is not required to provide any reasons for not consenting to a request for redemption of Preferred Shares.
>
> …
>
> 7. The adoption of this Preferred Share Redemption Policy does not fetter the discretion of the Director from time to time to amend or cancel this policy in whole or in part or to adopt an alternative policy with respect to the redemption of Preferred Shares, or to refuse to consent to a Requesting Shareholder's request to have their Preferred Shares redeemed by the Company.

[118] Another redemption policy (undated) in evidence from Mr. Bergman, attached as Exhibit "D" to his affidavit sworn November 7, 2017, is to a similar effect, making it clear that redemptions may not be honoured:

> **Redemption of Preferred Shares:**
>
> The Company has adopted a policy regarding the redemption of Preferred Shares. A copy of such policy is available from the Company upon request. Pursuant to such policy, a Preferred Share will be redeemable by the Company in certain circumstances. **Although the Company will use its best commercial efforts to ensure that all requests for redemption are fulfilled, depending on such circumstances the Company cannot guarantee that any or all of the Preferred Shares in respect of which requests for redemption are received will be redeemed in any given fiscal year.**

…

> The adoption of its policy regarding the redemption of Preferred Shares does not fetter the discretion of the Directors of the Company from time to time to amend or cancel such policy in whole or in part or to adopt an alternative policy with respect to the redemption of Preferred shares, or to refuse to consent to a Requesting Shareholder's request to have their Preferred Shares redeemed by the Company.
>
> **There are times when redemption requests may not be processed in a timely manner and shareholders may have to wait longer than expected to receive their redemption request. The source of funds used to process redemptions may be from new capital raised and/or loans being repaid. There is no guarantee that funds will be available to meet all redemption requests.**
>
> [All emphasis in original.]

Unsatisfied Redemption Requests Are Not Debt

[119] The redeeming preferred shareholders place great importance on the decision of the Court of Appeal in *Re East Chilliwack Agricultural Cooperative* (1989), 74 C.B.R. (N.S.) (B.C.C.A.), to support their claim to be debt claimants when they delivered their redemption notices. The decision in that case has been the subject of adverse comment or distinguished in other case authorities in this province and others. However, it is sufficient for my determination to note that the facts of that case are clearly distinguishable from the instant proceeding.

[120] In that case, farmers who owned shares in an agricultural cooperative gave notice to the co-op of their intention to have their shares redeemed. Thereafter, and before they were paid, the Superintendent of Co-operatives suspended the right of the co-op to redeem its shares due to liquidity issues. Mr. Justice Hutcheon, writing for the majority, determined that they were entitled to be treated as creditors. However, as is noted at the outset of his reasons, the effect of the Superintendent's order was not argued on the appeal. More importantly for the issues raised on the present application, by virtue of the Cooperative's constating documents, the claimant shareholders in *East Chilliwack*, ceased to be shareholders when they served their redemption notices.

[121] As previously discussed, in the case at bar, redeeming preferred shareholders whose redemption requests were not honoured, either in whole or in

part, retained their rights and privileges as shareholders. They continued to receive a share of the profits of ACIC from dividend payments through to 2016. Also unlike *East Chilliwack*, ACIC's obligation to honour the redemption notices and to buy back shares remained discretionary throughout. In the present case, ACIC's obligation to redeem was always premised, at a minimum, on a best efforts basis and dependent on its liquidity.

[122] Thus, the decision in *East Chilliwack* is not authority for a general proposition that unpaid redemption requests are *indicia* of debt. Unsatisfied redemption requests do not of themselves change the substance of the relationship from an equity interest to a debt claim. In *Central Capital*, the preferred shareholders' claim that they were debt claimants on the basis of their unsatisfied rights of redemption was rejected by the majority: paras. 97, 135-136.

[123] In some instances, ACIC made partial payment of a redemption request and indicated in documents provided to certain redeeming preferred shareholders that the remaining unpaid redemption amounts were "o/s", or outstanding. During oral submissions, the possibility was raised that this advice from ACIC might reflect a change in the relationship between those particular redeeming shareholders and the company. In my opinion, it does not. In *Bul River*, the fact that redeeming shareholders had gone one step further and obtained judgment to recover unpaid redemption amounts was insufficient to convert their equity interest to a debt claim.

Winding-Up Provisions Do Not Affect the Result

[124] The redeeming preferred shareholders rely on the decision in *Coast Capital*, which treated similar winding up language in the Articles as *indicia* of a debt relationship, to support their position that they are debt claimants.

[125] I disagree that the reasons in *Coast Capital* support the position articulated by the redeeming preferred shareholders.

[126] At issue in that case was the tax treatment of shares issued by the credit union labelled "non-equity shares". The case involved statutory interpretation of provisions in the *Corporation Capital Tax Act*, R.S.B.C. 1996, c. 73, the *Financial*

Institutions Act, R.S.B.C. 1966, c. 141 [*FIA*], and the *Credit Union Incorporation Act*, R.S.B.C. 1996, c. 82, as well as the certain provisions of the rules promulgated by Coast Capital respecting the impugned shares (described as "non-equity" shares). Disimilar to the case at bar, the *FIA* defines a non-equity share (in s. 1(1)) issued by a credit union as one evidencing indebtedness of the credit union to the holder of the share that does not represent an equity interest in the credit union.

[127] The outcome in *Coast Capital* turned on its own facts, which are significantly different and thus distinguishable from the case at bar. For example, and unlike the case at bar, the shares in issue in *Coast Capital* were restricted to a 6% non-cumulative dividend in addition to the amount paid on winding up or dissolution. In addition, the credit union was required to redeem those shares on a fixed date. The Court of Appeal engaged in an analysis of the legal substance of those shares and determined that they reflected a debt interest.

[128] The statutory objectives and considerations in that case also differ from those concerning the *CCAA*. In her reasons in *Coast Capital*, Newbury J.A. observed that the case before the Court of Appeal did not concern bankruptcy of insolvency law: paras. 7, 53-56.

[129] In the case at bar, and unlike *CDIC*, there is no provision in the Articles or Offering Memoranda stating or even suggesting that upon a winding-up or insolvency, ACIC's preferred shareholders, let alone any who have sought redemption, are entitled to rank *pari passu* with its creditors: *CDIC* at 563; *Central Capital* at para. 132.

[130] Section 27.5 of the Articles provides a procedure for distribution of ACIC's assets upon winding up or liquidation. ACIC's assets will be distributed to the Preferred Shareholders in priority to the Common Shareholders as follows:

> Upon the winding up or dissolution or liquidation of the Company, the Company's assets will be distributed to the Preferred Shareholders in priority to the Common Shareholders as follows:
>
> - first to the Preferred Shareholders on a pro rata basis among the Preferred Shareholders until each Preferred Shareholder has received the lesser of: (i) the original subscription price for each Preferred

> Share for which the Preferred Shareholder is the registered holder and all dividends that have been declared but for which the Preferred Shareholder has yet to be paid; and (ii) the book value of the Preferred Shares, for which the Preferred Shareholder is the registered holder, as determined in the upcoming year-end audited financial statements; and
>
> - the balance to the Common Shareholders on a pro rata basis among the Common Shareholders, to the exclusion of the Preferred Shareholders.

[131] In *Central Capital*, Weiler J.A. pointed out that winding up and liquidation are other forms of insolvency. Both, she said, are "methods for secured creditors to enforce their claims by seizing the assets in which they hold security interests": para. 99. In the same paragraph, however, she said that in light of s. 173 of the governing statute in that case - the *Canada Business Corporations Act*, R.S.C., 1985, c. C-44 - whose provisions are similar to those found in Part 9 of the *BCA*, the interests of preferred shareholders with redemption rights are subordinated to creditors.

[132] Laskin J.A. took a similar view. As is the case in the instant proceeding, he found that even after redemption rights are exercised, preferred shareholders continue to be entitled to dividends until their shares are in fact redeemed. On a liquidation, shareholders rank as equity claimants and not as creditors (even though in that case, and unlike the facts of this case, their redemption rights allowed shareholders to compel the company to redeem so long as it was solvent). Redemption, Laskin J.A. explained, is a return of capital not a repayment of a loan: paras. 134-135.

[133] The same view was taken in *Nelson Financial* at para. 31(c).

No Alteration to Establish a Contractual Right to Compel Redemption Exists

[134] In their alternative argument, the redeeming preferred shareholders submit that if they were equity claimants at the outset, then their contractual relationship with ACIC changed as a result of its later redemption policies and certain communications that ACIC published or delivered to potential and existing

shareholders. They submit that ACIC's redemption policies moved away from a discretionary right held by Mr. Bergman and became an enforceable contractual right held by each preferred shareholder to compel redemption during specific windows of time and upon certain conditions being met.

[135] I disagree. The redeeming preferred shareholders have not established that their contractual relationship with ACIC changed so as to become debt creditors.

[136] The redemption policies that ACIC issued starting in 2006 did not provide an unconditional promise that redemption notices would be honoured. Those policies were clear that ACIC's right to honour a redemption request was always at the discretion of its directors.

[137] The communcations from ACIC also do not alter the contractual relationship. The examples provided by the redeeming preferred shareholders consist, for the most part, of marketing materials, executive summaries, and standard form answers to "FAQs" (frequently asked questions). Many of the impugned communications appear on their face to be intended to induce investment in ACIC through subscriptions of Units.

[138] ACIC's communications do not convey an intention to enter into a binding agreement: *Aubrey v. Teck Highland Valley Copper Partnership*, 2017 BCCA 144 at paras. 47- 48.

[139] As I have found, ACIC's communications with its preferred shareholders concerning redemptions and redemption policies and terms were clearly stated throughout to be subject to the sole discretion of its directors. ACIC continued to make it clear to its preferred shareholders throughout that in addition to its right to refuse to honour a redemption request, it retained the right to alter, amend, or cancel its redemption policy at any time. In some communications, ACIC advised that its ability to honour a redemption request depends on the company's liquidity.

[140] Each preferred shareholder was required to sign a Subscription Agreement in order to purchase Units. They contained language confirming the subscriber's

decision to purchase Units was based solely upon the information contained in the Offering Memoranda and any agreements or documents incorporated in them. There is no room to incorporate into the Subscription Agreements any representations that might have been made and relied upon by the redeeming preferred shareholders either at the time of subscription or afterward.

[141] ACIC's redemption policies and communications cannot purport to change the rights attached to shares, such as redemption rights, as set out in the Articles, which is a foundation document governing the contractual rights of preferred shareholders. The Articles can only be amended by special resolution and in strict compliance with the *BCA*, which did not occur in this case: *BCA*, ss. 2(2)(b), 54(3), 58(2), 61. For example, s. 61 of the *BCA* provides that special rights and restrictions attached to a share are not varied or deleted until a company's articles have been altered to reflect the variation or deletion:

> 61. A right or special right attached to issued shares must not be prejudiced or interfered with under this Act or under the memorandum, notice of articles or articles unless the shareholders holding shares of the class or series of shares to which the right or special right is attached consent by a special separate resolution of those shareholders.

[142] Further, based on the evidence adduced on this application, mass communications sent from or given by ACIC to potential and existing preferred shareholders do not establish a change in the relationship.

[143] In any event, even if it could be said that there was an elimination of unfettered and at will discretion to redeem on the part of ACIC's director, the substance of the relationship between ACIC and its preferred shareholders did not change from equity to debt as a result.

[144] Lastly, it is not an issue on this application whether the redeeming preferred shareholders can look beyond the four corners of their Subscription Agreements, such as to advance a claim for inducement to purchase shares or any delay in requesting a redemption through a representation(s) made by on or behalf of ACIC. The answer to that question also has no bearing on the characterization of the

nature of the redeeming preferred shareholders' status in this *CCAA* insolvency proceeding.

[145] For these reasons, I do not need to consider the redeeming preferred shareholders' submission, based on *Rosas v. Toca*, 2018 BCCA 191, that no consideration is necessary to support the alleged change in their contractual relationship with ACIC.

Treatment in Financial Records

[146] Since surrounding circumstances are referred to by the redeeming preferred shareholders, it is useful to refer to the manner in which ACIC treated its preferred shareholders in its financial records. Reference to treatment in financial records was considered in some of the case authorities I have cited (e.g., *Central Capital*). In considering this evidence, I am mindful of the caution in *CDIC* (at para. 61) that a company's treatment in its financial records is to be accorded limited weight.

[147] ACIC's financial records describe the preferred shares as "Share Capital" and not as debt. There are separate, specific line items for short term and long term debt and debentures, which do not include the monies paid by subscribers for their Units. For example, the 2015 financial statements state that there is "No Long Term Debt". Capital from share subscriptions is described as "Shareholders' equity" in financial statements prepared by ACIC's third party accounting firm, BDO Dunwoody, under a line item entitled, "Liabilities and Shareholders' Equity".

Conclusion

[148] The preferred shareholders' investment in ACIC was in respect of an equity interest. Their claims are not debt claims. They are claims that only a shareholder can make. The redemption rights attached to ACIC's preferred shares are in substance rights to the return of a capital invested in a MIC with significant risks.

[149] ACIC's deteriorating financial position led to its inability to honour the outstanding redemption requests delivered by certain preferred shareholders. It is a

risk that all preferred shareholders were clearly informed of before purchasing their shares.

[150] A declaration shall issue that the claims of all of its preferred shareholders fall within the ambit of equity claims as defined in s. 2 of the *CCAA*.

"Walker J."

_____

The Honourable Mr. Justice Walker

TAB 11

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Bul River Mineral Corporation (Re),* 2014 BCSC 1732

Date: 20140915
Docket: S113459
Registry: Vancouver

In the Matter of the *Companies Creditors Arrangement Act*, R.S.C. 1985, c. C-36 as amended

And

In the Matter of the *Business Corporations Act,* S.B.C. 2002, c. 57 and the *Business Corporations Act*, R.S.A. 2000, c. B-9

And

In the Matter of Bul River Mineral Corporation, Big Bear Metal Mining Corporation, Earth's Vital Extractors Limited, Fort Steele Mineral Corporation, Fort Steele Metals Corporation, Fused Heat Ltd., Gallowai Metal Mining Corporation, Giant Steeples Mineral Corporation, Grand Mineral Corporation, International Feldspar Ltd., Jao Mine Developers Ltd., Kutteni Diamonds Ltd., Stanfield Mining Group of Canada Ltd., Sullibin Mineral Corporation, Sullibin Multi Metal Corporation, Super Feldspars Corporation, White Cat Metal Mining Corporation, Zeus Metal Mining Corporation, Zeus Metals Corporation and Zeus Mineral Corporation

Petitioners

Before: The Honourable Madam Justice Fitzpatrick

Reasons for Judgment

Counsel for the Petitioners:	Colin D. Brousson
Counsel for CuVeras, LLC:	William C. Kaplan, Q.C. Peter Bychawski
Counsel for Eldon Clarence Stafford	J. Roger Webber, Q.C.
Counsel for Gordon Preston and Carol Preston	Robert M. Curtis, Q.C.

Counsel for the Monitor, Deloitte Restructuring Inc.	Tevia R.M. Jeffries
Place and Date of Hearing:	Vancouver, B.C. September 3 and 5, 2014
Place and Date of Judgment:	Vancouver, B.C. September 15, 2014

Introduction

[1] These are longstanding proceedings under the *Companies' Creditors Arrangement A*ct, R.S.C., 1985, c. C-36 (the "*CCAA*"), having been commenced some three and a half years ago in May 2011. Since that time, the petitioners have made slow and steady progress toward the goal of presenting a plan of arrangement to their creditors and certain equity participants.

[2] The principal petitioners, being Bul River Mineral Corporation ("Bul River") and Gallowai Metal Mining Corporation ("Gallowai"), are the owners of certain mining properties and related assets in the Kootenay region of British Columbia. As a result of these proceedings, Bul River and Gallowai now have some indication that the mine is viable. This has been accomplished mainly due to the participation of CuVeras, LLC ("CuVeras") who has, since late 2011, provided interim financing which allowed this further development work to continue to this point in time.

[3] Some years ago, Bul River and Gallowai completed a claims process to identify not only trade creditors but also claims of its common and preferred shareholders. Now that Bul River and Gallowai, with the assistance and sponsorship of CuVeras, are on the cusp of preparing a plan of arrangement for consideration by the stakeholders, those claims have become of central importance.

[4] Some of the claims that were advanced through the claims process were not critically considered by either the petitioners or the court-appointed monitor, Deloitte Restructuring Inc. (the "Monitor"). However, at this late date, the characterization of certain claims and the validity of certain claims have been put in issue and will have a profound impact on the manner in which these restructuring proceedings go forward.

[5] At present, the general intention is that the restructuring will take place along the lines of a Letter of Agreement between the petitioners and CuVeras dated May 23, 2014. By that agreement, a newly formed British Columbia entity ("Newco") will be created and the shares in Newco will be distributed to CuVeras and other related parties and also to non-voting preferred shareholders. Trade creditors will also

participate in Newco. This Letter of Agreement is the product of some history, sometimes contentious, between the petitioners and CuVeras which was discussed in the court's earlier reasons: *Bul River Mineral Corporation (Re)*, 2014 BCSC 645.

[6] One of the claims is that advanced by Gordon and Carol Preston (the "Preston Claim"), which CuVeras contends is an equity claim as opposed to a debt claim. Another claim is that advanced by Eldon Stafford (the "Stafford Claim"), which CuVeras contends is not a valid claim against Bul River or Gallowai. The substance of the issue before the court therefore is two-fold: (a) the proper categorization of the Preston Claim and (b) whether the Stafford Claim is a valid claim against the petitioners.

[7] As will become apparent from the discussion below, the resolution of these issues will significantly impact how any restructuring plan can be crafted and will also impact all stakeholders in terms of how the Newco shares will be distributed between the various stakeholders. There is some urgency in resolving these last issues before the restructuring can proceed. All involved, including the Monitor, state that it is necessary for the petitioners to exit this *CCAA* proceeding as quickly as possible. At this time, a plan of arrangement sponsored by CuVeras is the only option available to the petitioners so as to avoid a liquidation and bankruptcy.

Background

[8] The petitioners are also known as the Stanfield Mining Group (the "Group"). The Group carried on the business of developing a mining property situated near the Bull River just outside of Fernie, British Columbia. It is effectively controlled by the estate of Ross Stanfield ("Stanfield") which holds 100% and 99.9% of the voting common shares in the parent companies, Zeus Mineral Corporation and Fort Steele Mineral Corporation, respectively. As stated above, the two principal companies involved in the development and operation of the mine within the Group are Bul River and Gallowai.

[9] The mine, known as the Gallowai Bul River Mine, is not currently in production. There has been significant underground development to this point such

that the petitioners and CuVeras consider that with a relatively modest further investment the mine could be placed into production.

[10] Bul River and Gallowai were incorporated in the 1980s. Commencing in the mid-1990s, Stanfield began raising funds for the development of the mine. The marketing program focused on "sophisticated investors" which are, through securities regulation statutes, defined as persons with a net worth in excess of $1 million willing to invest a minimum of $100,000 in a given venture. The persons targeted by Stanfield's marketing campaign were farmers in Alberta, particularly around Edmonton, Red Deer and Medicine Hat, as well as farmers from the area around Regina, Saskatchewan.

[11] Until 2010, Stanfield engaged in a sophisticated marketing program to sell redeemable preferred non-voting shares to these investors. Over that period of time, approximately $229 million was invested in consideration of which preferred shares in Bul River and Gallowai were issued.

[12] The marketing program involved repeated representations as to the ore content of the mine. Stanfield continually referred to the mine as an "elephant" mine, meaning that the mineral resources were enormous. Over the years, the program included visits to the mine site and presentations to potential investors by Stanfield. Those presentations referred to the history of the mine and the future prospects of the mine, including development plans and the levels of ore content (copper, gold and platinum). The presentations also involved discussion as to when production would commence and typically production was forecast to commence within a foreseeable period of time, be it one or two years from the date of the meeting.

[13] The same representations were also made in written materials, including a report from Phillip De Souza ("De Souza"), a professional engineer.

[14] Some potential investors executed subscription agreements for shares during those visits to the mine or immediately thereafter. Some returned to the mine for

subsequent tours and subsequent purchases. In some instances, Stanfield recruited current investors to further market the preferred shares to other investors.

[15] These representations by Stanfield were made in the face of contemporaneous reports which questioned the value of the resources announced by the Group. These included papers published by the British Columbia Ministry of Energy and Mines in 2000 in which it was reported that they were unable to confirm the gold grades reported by the Group. In 2006, a professional conduct hearing in Alberta was held arising from charges that De Souza's report was "deficient and misleading". The panel issued reasons which were published in January 2008 in which it concluded that De Souza's conduct constituted unskilled practice and unprofessional conduct.

[16] Eventually, Stanfield's activities caught the attention of various provincial securities regulators. In May 2010, the British Columbia Securities Commission (the "Commission") issued a Notice of Hearing against Stanfield, Bul River and Gallowai seeking to order them to produce an independently prepared technical report fully compliant with NI 43-101 (Standards of Disclosure for Mineral Projects) that would include an estimate of the mineral resources available at the mine.

[17] Ross Stanfield died on August 3, 2010.

[18] By the fall of 2010, in addition to being faced with the Commission proceedings, certain preferred shareholders had taken legal action against the Group in light of the failure to comply with redemption obligations arising in respect of the preferred shares. Stanfield's grandson, George Hewison, is the sole beneficiary of Stanfield's estate. He stepped in to continue the work of the Group as best he could. In late 2010 or early 2011, undertakings were given to the securities regulators in British Columbia and Alberta by which the petitioners agreed not to issue any new securities without their consent.

[19] The evidence would later establish that the representations made by Stanfield regarding the mine resources were false. A technical report was later prepared by

Rosco Postle and Associates Inc. ("RPA") in March 2011 that provided some review of the available mineral resources at the mine. Both the RPA report and a later report prepared by Snowden Mining Industry Consultants in March 2013 would indicate that while there is valuable ore in the mine, the quantity of the resources is markedly less than what was indicated in the representations made to investors.

[20] On May 26, 2011, the Group sought and obtained creditor protection pursuant to the *CCAA* and an Initial Order was granted at that time.

[21] At the time of the *CCAA* filing, the Class A common voting shares in Bul River and Gallowai were held by the Stanfield estate. Other Class B and Class E common non-voting shares were held by investors.

[22] As of the date of filing, the petitioners had no secured creditors. The petition referenced debt obligations of $904,000 to trade suppliers and two unsecured judgments totalling $386,135. Various preferred non-voting shares were held by investors in Classes C, D and F. The petition materials indicated that amounts owing for "redeemable shares" (i.e., the preferred shares) were approximately $137,718,557. The holders of both common and preferred shares comprise some 3,500 individual investors.

[23] The subscription agreements for the preferred shares provided that the shares were redeemable at the end of five years from the date of the subscription together with a "preferred cumulative annual dividend" of 12.75%. There is no evidence of any significant redemption of the preferred shares. Rather, as redemption dates arose, preferred shareholders were approached to execute extension agreements extending their redemption rights from a given date to a date defined by the commencement of production from the mine. Many preferred shareholders signed those extension agreements, some did not. For those who did not, some of them demanded redemption of their shares. For the most part, those investors were told that there was no money to redeem the shares.

[24] Accordingly, the largest liability faced by the petitioners is that arising from the preferred shares. The preferred shareholders appear to have certain claims arising from their holdings. Firstly, they have a claim for payment of the redemption amount plus the accumulated dividend. Secondly, they may have a claim for misrepresentation against the Group, giving rise to potential remedies of rescission of their subscription agreements, damages, or both.

The Claims Process

[25] In August 2011, the Group prepared a list of creditors (the "Creditor List") in support of seeking a claims process order. The list actually included not only trade claims but also shareholder claims. Not surprisingly, the purpose of the claims process was to assist the Group in developing its restructuring plan.

[26] On August 19, 2011, the court approved a Claims Process Order, which authorized the petitioners to conduct a claims process for the determination of any and all claims against them (the "Claims Process"). The Claims Process Order defined "claims" that were to be determined in the Claims Process as follows:

> … indebtedness, liability or obligation (including an equity obligations arising from the ownership of equity shares) …
>
> … all obligations of or ownership interests in the Petitioners or any of them arising from or relating to the holding of a Share.

[27] Under the Claims Process Order, all "Known Creditors" (defined in the Claims Process Order as all creditors shown on the books and records of the petitioners as having a claim in excess of $250), including holders of shares, were to receive a claims package from the petitioners that included an instruction letter, a Notice of Dispute, a Proof of Claim, and a copy of the Claims Process Order (the "Claims Package"). The Claims Process was also advertised in certain publications. The Creditor List indicating such Known Creditors was posted on the Monitor's website, as was noted in the Claims Package, such that both creditors and shareholders were able to view it. The process of determining claims was as follows:

a) all creditors and shareholders were given the opportunity to review the Creditor List;

b) in the event a creditor or shareholder agreed with the "Claim Particulars" listed in the Creditor List (which included the number and class of shares), the creditor or shareholder did not need to file a Proof of Claim with the petitioners. In that event, the Claim Particulars in the Creditor List would be deemed to be the creditor or shareholder's proven claim for voting and distribution purposes under any restructuring plan subsequently filed by the petitioners;

c) in the event a creditor or shareholder objected to the Claim Particulars in the Creditor List, or wished to advance another claim, the creditor or shareholder had to, on or before October 17, 2011 (the "Claims Bar Date"), deliver to the petitioners, with a copy to the Monitor, a notice of such objection in the form of a Notice of Dispute, together with a Proof of Claim and supporting documentation;

d) in the event a Notice of Dispute was not submitted on or before the Claims Bar Date, the creditor or shareholder was deemed to have accepted the amount owing and all other Claim Particulars set out in the Creditor List, and was forever barred from advancing any other claim against the petitioners or participating in any plan subsequently filed by the petitioners;

e) where a Notice of Dispute and/or Proof of Claim was filed by a creditor or shareholder, the petitioners were deemed to have accepted it unless they delivered to the creditor or shareholder a Notice of Disallowance on or before October 31, 2011 (later extended to November 15, 2011); and

f) in the event of the petitioners delivering a Notice of Disallowance, a creditor or shareholder had 21 days to seek a determination from the court of the validity and value of and particulars of the claim by filing and serving

> the petitioners and the Monitor with application materials. A creditor or shareholder who failed to file and serve such materials by the deadline was deemed to have accepted the particulars of its claim set out in the Notice of Disallowance.

[28] The Claims Process Order did not contemplate the appointment of a claims officer or the participation of the Monitor in the process of assessing the validity of the Proofs of Claim and/or Notices of Dispute submitted to the petitioners through the Claims Process. Nor did the Claims Process allow any independent review of claims submitted by other creditors of the petitioners or by CuVeras as the interim financier.

(i) Jurisdiction of the Court

[29] Before turning to claims process orders specifically, it is important to keep in mind the broad remedial objectives of the *CCAA* to facilitate a restructuring rather than a liquidation of assets: *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60 at paras. 15-18, 56. As the Supreme Court of Canada has noted, it is now well recognized that a supervising judge of a *CCAA* proceeding has a "broad and flexible authority" or statutory jurisdiction to makes such orders as are necessary to achieve those objectives: *Century Services* at paras. 19, 57-66.

[30] The discretionary authority of the court is confirmed by s. 11 of the *CCAA* which provides that the court may make any order that it considers "appropriate in the circumstances". As Madam Justice Deschamps observed in *Century Services*, whether an order will be appropriate is driven by the policy objectives of the *CCAA*:

> [70] The general language of the *CCAA* should not be read as being restricted by the availability of more specific orders. However, the requirements of appropriateness, good faith, and due diligence are baseline considerations that a court should always bear in mind when exercising *CCAA* authority. Appropriateness under the *CCAA* is assessed by inquiring whether the order sought advances the policy objectives underlying the *CCAA*. The question is whether the order will usefully further efforts to achieve the remedial purpose of the *CCAA* — avoiding the social and economic losses resulting from liquidation of an insolvent company. I would add that appropriateness extends not only to the purpose of the order, but also to the means it employs. Courts should be mindful that chances for

> successful reorganizations are enhanced where participants achieve common ground and all stakeholders are treated as advantageously and fairly as the circumstances permit.

[31] Claims process orders are an important step in most restructuring proceedings. In *Timminco Limited (Re)*, 2014 ONSC 3393, Mr. Justice Morawetz reviewed the "first principles" relating to claims process orders and their purpose within *CCAA* proceedings:

> [41] It is also necessary to return to first principles with respect to claims-bar orders. The CCAA is intended to facilitate a compromise or arrangement between a debtor company and its creditors and shareholders. For a debtor company engaged in restructuring under the CCAA, which may include a liquidation of its assets, it is of fundamental importance to determine the quantum of liabilities to which the debtor and, in certain circumstances, third parties are subject. It is this desire for certainty that led to the development of the practice by which debtors apply to court for orders which establish a deadline for filing claims.
>
> [42] Adherence to the claims-bar date becomes even more important when distributions are being made (in this case, to secured creditors), or when a plan is being presented to creditors and a creditors' meeting is called to consider the plan of compromise. These objectives are recognized by s. 12 of the CCAA, in particular the references to "voting" and "distribution".
>
> [43] In such circumstances, stakeholders are entitled to know the implications of their actions. The claims-bar order can assist in this process. By establishing a claims-bar date, the debtor can determine the universe of claims and the potential distribution to creditors, and creditors are in a position to make an informed choice as to the alternatives presented to them. If distributions are being made or a plan is presented to creditors and voted upon, stakeholders should be able to place a degree of reliance in the claims bar process.

[32] The overall objective of achieving certainty within the restructuring proceedings - for both debtor and creditor - is what drives this process. In this vein, counsel makes an effort to draft a claims process order to achieve these objectives. A claims bar date is typically set. The process is typically designed with some idea of the issues that either have arisen or might arise in the restructuring. My comments in *Steels Industrial Products Ltd. (Re)*, 2012 BCSC 1501 are apposite:

> [38] Similar issues often arise in *CCAA* proceedings where counsel and the Court must be mindful of issues that may arise in relation to the determination of claims in that proceeding. There are no set rules, but care must be taken in the drafting of the claims process order to ensure that the process by which claims are determined is fair and reasonable to all

> stakeholders, including those who will be directly affected by the acceptance of other claims. In *Winalta Inc. (Re)*, 2011 ABQB 399, Madam Justice Topolniski stated that "[p]ublic confidence in the insolvency system is dependent on it being fair, just and accessible".
>
> [39] Many *CCAA* proceedings provide for an independently run claims process (for example, by the monitor), the cost of which again would be borne by the general body of creditors: see for example, *Pine Valley Mining Corp. (Re)*, 2008 BCSC 356. To this extent, the statutory procedure under the *BIA* and the claims process under the *CCAA* will have similar features, which is understandable since the overriding intention under both is to conduct a proper claims process: see *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60 at paras. 24 and 47.

[33] Nevertheless, issues can and do arise that no one is able to foresee at the time of the claims process order. In that event, the court retains its discretion to address the application of the claims process order: *Timminco* at para. 38. In that case, the claims process order specifically allowed the court to order a further claims bar date. No such provision is found in the Claims Process Order but I do not consider that its absence is sufficient to oust the statutory jurisdiction of the court in appropriate circumstances.

[34] This, of course, is a different issue in that by the failure of the petitioners to deliver a Notice of Disallowance in respect of the claims in issue, they were deemed to have been accepted by the petitioners. This is not a case where a creditor is seeking to avoid the consequences of not filing materials by the time of the Claims Bar Date. Nevertheless, in my view, the court still retains the statutory jurisdiction to consider the validity of claims that might otherwise, by the Claims Process Order, be deemed to have been accepted.

[35] The Prestons and Mr. Stafford do not suggest that the court lacks the jurisdiction to reconsider the issues that arise in relation to their claims. The Prestons do, however, contend that it is not appropriate that any reconsideration take place at this time.

(ii) Review of the Claims

[36] The stated purpose of the *CCAA* is to facilitate compromises and arrangements between companies and their creditors (see also s. 6 of the *CCAA*). In

accordance with that fundamental objective or purpose, it is axiomatic that it is necessary to determine what are the true claims of the creditors as might be compromised or arranged.

[37] A "creditor" is not defined in the *CCAA*, unlike the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c.B-3 (the "*BIA*") where it is defined as meaning "a person having a claim provable as a claim" under that *Act* (s. 2). Both the *CCAA* and the *BIA* define "claim" by reference to liabilities "provable" under the *BIA*. Specifically, s. 2(1) of the *CCAA* defines "claim" as meaning:

> any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the *Bankruptcy and Insolvency Act*.

Section 2 of the *BIA* defines a "claim provable in bankruptcy" as "any claim or liability provable in proceedings under this Act by a creditor".

[38] Section 121(1) of the *BIA* addresses which claims are "provable claims":

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

[39] In substance, this same statutory definition is applied in the *CCAA* and represents a point of convergence consistent with the harmonization of certain aspects of insolvency law under both the *CCAA* and *BIA*: *Century Services* at para. 24. In addition, as noted by CuVeras, this definition is essentially used in the Claims Process Order by its definition of "Claim".

[40] Various authorities establish that a "provable debt" must be due either at law, or in equity, by the bankrupt to the person seeking to prove a claim and must be recoverable by legal process: *Excelsior Electric Dairy Machinery Ltd. (Re)*, [1923] 2 C.B.R. 599 (Ont. S.C.), 3 D.L.R. 1176; *Farm Credit Corporation v. Dunwoody Limited,* [1988] 68 C.B.R. (N.S.) 255 (Alta. C.A.), 51 D.L.R. (4th) 501, leave to appeal to S.C.C. refused, 73 C.B.R. (N.S.) xxvii (note), 100 60 D.L.R. (4th) vii (note);

Central Capital Corp. (Re), [1995] 29 C.B.R. (3d) 33 (Ont. Gen. Div.), O.J. No. 19 ("*Central Capital*"), aff'd [1996] 27 O.R. (3d) 494 (C.A.), 38 C.B.R. (3d) 1 ("*Central Capital* (ONCA)"); *Negus v. Oakley's General Contracting* (1996), 40 C.B.R. (3d) 270 (N.S.S.C.), 152 N.S.R. (2d) 172.

[41] In a *CCAA* proceeding, a claims process order is the means by which the "claims" of the creditors are determined. By reason of that process, the debtor is able to determine the nature and extent of its debts and liabilities so as to enable it to formulate a plan of arrangement. There are no rules as to when a claims process may be implemented although it is usually early in the process in anticipation of a plan and distributions to creditors. In that respect, a debtor company will be seeking some certainty regarding the determination of claims for that purpose.

[42] In *Timminco*, the Court, prior to citing relevant authorities at para. 52, outlined many of the factors that might be considered by the court in relation to deciding whether to allow claims to be advanced after the claims bar date:

> [51] Counsel to Mr. Walsh submit that courts have historically considered the following factors in determining whether to exercise their discretion to consider claims after the claims-bar date: (a) was the delay caused by inadvertence and, if so, did the claimant act in good faith? (b) what is the effect of permitting the claim in terms of the existence and impact of any relevant prejudice caused by the delay[?] (c) if relevant prejudice is found, can it be alleviated by attaching appropriate conditions to an order permitting late filing? and (d) if relevant prejudice is found which cannot be alleviated, are there any other considerations which may nonetheless warrant an order permitting late filing?

[43] As I have stated above, the broad jurisdiction of the court under s. 11 of the *CCAA* allows the court to make such orders as are "appropriate". While the above factors have been considered in the past, there is no finite list that detracts from a consideration of all relevant circumstances. Nevertheless, the general considerations of delay and prejudice typically arise, just as they do in this case.

[44] I return to the factual circumstances relating to the Claims Process and the Claims Process Order. The petitioners were themselves responsible for reviewing the Proofs of Claim and/or Notices of Dispute submitted in the Claims Process. The

principal individual involved in the review was Mr. Hewison who did so with the assistance of counsel. It is apparent that the only factors considered in his review included whether a claim related to a trade debt or whether it related to an equity interest in the petitioners.

[45] The Prestons argue that the Claims Process was well known to everyone and that its purpose was to establish the amount and nature of all claims. This is clearly self-evident, but back in late 2011, it was the case that the course of the restructuring proceedings was anything but certain. In fact, the ability of the petitioners to continue the proceedings was tenuous and they were scrambling to find interim financing which they eventually secured with CuVeras in November 2011. By that time, the Claims Process was essentially completed. Even so, understandably, the parties were concerned to proceed as quickly as possible to obtain further technical reports on the proven or inferred mine resources in order to determine whether a viable mine even existed. They did receive those later reports, which included a further RPA report and the Snowden report. In these circumstances, Mr. Hewison did not undertake any substantive review of the claims.

[46] The Prestons further say that, since they faithfully complied with the Claims Process Order, it would be patently unfair to now revisit the characterization of their claim. While they raise the matter of the three year plus delay, no elements of prejudice have been alleged. In my view, the delay, while relevant, will have little effect on the ability of the parties to address the substance of the matter. Nor have any rights been extinguished or compromised by reason of any delay. Accordingly, the objective of certainty has less force in this case where the plan of arrangement has yet to be formulated and the claimants have yet to consider that plan and vote on it. I note that similar considerations were at play in *Timminco* where it was apparent that no plan would ever be put to the creditors.

[47] Finally, the Prestons argue that the Claims Process Order constituted the sole form of adjudication of the validity and nature of the claims submitted. It is true, of course, that the petitioners had an opportunity to consider these claims.

[48] As discussed below, the petitioners did not forward any Notice of Disallowance in respect of the Proofs of Claim later filed by the Prestons and Mr. Stafford. Mr. Hewison considered that the Stafford Claim should be categorized as an "investment" in the mine. Further, with respect to the Preston Claim, he was not aware of the significance of the distinction between an equity claim and a debt claim. In retrospect, and now knowing what type of plan of arrangement is possible, Mr. Hewison recognizes that this was in error. It appears that a combination of factors - including Mr. Hewison's lack of familiarity with the past transactions, inadequate record keeping, lack of resources and distraction in terms of larger issues more relevant to the survival of the mine - all contributed to a less rigorous review and analysis of these claims.

[49] It is the case, however, that the petitioners were acting in good faith, albeit without a full appreciation of the issues arising in respect of these claims and the also the consequences of their inaction.

[50] More importantly, aside from the petitioners, other stakeholders have a significant interest in whether a claim is valid or not and that any claim be properly characterized. Based on the anticipated form of the restructuring plan, the inclusion of the Stafford Claim and characterization of the Preston Claim will impact the recovery of these stakeholders. These other creditors or stakeholders of the petitioners did not have any opportunity up to this point in time to review the claims. I would again note that the Claims Process Order did not contemplate any review of the claims by these other stakeholders, such as was the case in *Steels Products* (see paras. 13-15).

[51] Nor has the Monitor participated in any review of these claims. I do not say this as any criticism of the Monitor as the Claims Process Order did not expressly provide for any such independent review. Nor does the Claims Process Order contemplate that any other independent review of the claims be completed which might have highlighted the issues. The Monitor did report on the Claims Process from time to time (particularly, its report from June 2012 and January 2013),

however, no such issues were identified. As such, the Monitor did not conduct a critical review of the claims, similar to what a trustee in bankruptcy might have done under s. 135 of the *BIA*.

[52] In these circumstances, and in retrospect, the Claims Process lacked procedural safeguards that might have avoided this problem: *Steels Products* at paras. 38-39.

[53] In these circumstances, I disagree with the Prestons that the Claims Process Order constitutes an adjudication of these issues by which CuVeras or any other stakeholder is estopped in bringing these issues forward. It is clear that to this point, no such adjudication has occurred.

[54] As I have indicated above, a Claims Process Order is intended to be a fair, reasonable and transparent method of determining and resolving claims against the estate. In certain circumstances, these objectives fail to be achieved through no fault of the participants. That does not preclude the court from considering the issues on their merits so as to achieve the fundamental objective under the *CCAA* to facilitate a restructuring based on valid claims. This would also include a consideration of the proper characterization of the Preston's claim: *Steels Products* at para. 42.

[55] Simply put, if the Claims Process results in a claim being advanced which is not truly a debt of the petitioners or results in a claim being improperly characterized, the fairness and transparency of these proceedings are inevitably compromised such that the objectives of the *CCAA* will not be fulfilled.

[56] My comments in *Steels Products* apply equally here:

> [46] In conclusion, an independent review of these claims is necessary in the circumstances. An adequate review of these related party claims has not been made. The consequences of a successful challenge to some or all of these claims would have significant financial repercussions to the Disputing Creditors and other unsecured creditors who have also proved their claims. To deny an independent review at this time would be to deny any creditor the fair, reasonable and transparent process that is expected in insolvency proceedings in determining claims before any distribution of estate assets is made.

[57] Even at this late stage in the proceedings, and considering the ongoing supervisory role of the court, I consider that it is appropriate to address the issues relating to both the Preston Claim and the Stafford Claim on their merits. This is particularly so given the significant repercussions to other stakeholders and the lack of any prejudice to the Prestons and Mr. Stafford.

Discussion

(a) The Preston Claim

[58] The Preston Claim is advanced as a debt claim in these proceedings, a position that is disputed by CuVeras who contends that in fact, it is an equity claim as defined in the *CCAA*.

(i) The Proof of Claim

[59] The Creditor List referenced the Prestons as holding various Class E (2,102) and Class F (2,400) preferred shares.

[60] In October 2011, the Prestons, through their counsel, submitted a Proof of Claim and Notice of Dispute.

[61] The genesis of the claim was as described in a Statement of Claim filed in the Alberta Court of Queen's Bench against Gallowai on May 27, 2010. The claim was as follows: in October 2004, the Prestons subscribed for 2,400 Class F preferred shares in Gallowai in consideration of the payment to Gallowai of $120,000; Gallowai is alleged to have covenanted to redeem the preferred shares at the expiry of five years after the allotment date; the Prestons demanded redemption of the shares and the payment of dividends which was to be by way of issuance of Class E shares; Gallowai refused to respond to their demands; and the Prestons claimed the right to redeem the Class F preferred shares for $120,000 plus either dividends in the form of Class E common shares or, alternatively, cash payment of dividends at 12.75% per annum.

[62] On November 19, 2010, default judgment was granted in favour of the Prestons for the claimed amount of $120,000 plus the cash dividend interest rate for

a total judgment of $214,527.10 including court ordered costs. The Prestons attempted to register their judgment in British Columbia in June 2011 after the court ordered a stay arising under the Initial Order, but nothing turns on that step.

[63] The Proof of Claim indicates that the Prestons were advancing both a trade claim for the judgment amount and also a claim for non-voting shares arising from the allegation that they continue to hold the 2,102 Class E shares noted on the Creditor List.

(ii) Historical Approach to Equity Claims

[64] Before I turn to the current statutory regime arising from amendments to the *CCAA* and *BIA* in 2009, I will review the authorities which applied before these amendments were enacted.

[65] Historically, equity and debt claims have been treated differently in an insolvency proceeding given the fundamental difference in the nature of such claims. That different treatment resulted in the subordination of equity to debt claims. The basis for this judicially developed principle was that equity investors are understood to be higher risk participants. Creditors, on the other hand, have been held by the courts to have chosen a lower level of risk exposure that should generally result in priority over equity investors in an insolvency context.

[66] In *Sino-Forest Corporation*, 2012 ONCA 816, affirming 2012 ONSC 4377, the Court of Appeal commented with approval on the analysis of Morawetz J. in the court below:

> [30] Even before the 2009 amendments to the CCAA codified the treatment of equity claims, the courts subordinated shareholder equity claims to general creditors' claims in an insolvency. As the supervising judge described [at paras. 23-25]:
>
> > Essentially, shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditor claims are not being paid in full. Simply put, shareholders have no economic interest in an insolvent enterprise.
> >
> > The basis for the differentiation flows from the fundamentally different nature of debt and equity investments. Shareholders have unlimited

> upside potential when purchasing shares. Creditors have no corresponding upside potential.
>
> As a result, courts subordinated equity claims and denied such claims a vote in plans of arrangement [citations omitted].

[67] See also *Central Capital* at paras. 41-42; *Central Capital* (ONCA) at 510-11, 519.

[68] In light of that key distinction, courts in the past have embarked upon a consideration as to the true characterization of certain claims in an insolvency context. There is considerable authority that in making that determination, the court will consider the true substantive nature or character of the claim, rather than the form of the claim.

[69] The leading case is the Supreme Court of Canada's decision in *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, [1992] 3 S.C.R. 558 ("*CDIC*"). In that case, the issue was whether money advanced to the debtor bank was in the nature of a loan or a capital investment for the purpose of determining whether the creditors advancing the funds ranked *pari passu* with other unsecured creditors in a winding-up proceeding. Mr. Justice Iacobucci stated that the approach was to determine the "substance" or "true nature" of the transaction (563, 588). His oft quoted statements are found at 590-91, the relevant principles of which can be summarized as follows:

a) the fact that a transaction contains both debt and equity features does not, in itself, determine its characterization as either debt or equity;

b) the characterization of a transaction under review requires the determination of the intention of the parties;

c) it does not follow that each and every aspect of a "hybrid" debt and equity transaction must be given the exact same weight when addressing a characterization issue; and

d) a court should not too easily be distracted by aspects of a transaction which are, in reality, only incidental or secondary in nature to the main thrust of the agreement.

[70] One type of financial instrument that typically has elements of both equity and debt are preferred shares, where arguably rights of redemption and rights to payment of dividends evidence debt characteristics.

[71] The issue of the characterization of preferred shareholder claims in an insolvency context was addressed in *Central Capital* (ONCA). In that case, the court had to characterize a claim arising from the right of retraction in respect of certain preferred shares. Although differing in the result, the majority opinions and the dissenting opinion at the appellate court level were consistent in an approach toward determining the *substance* of the claim in terms of whether it was a "provable debt". In dissent, Finlayson J.A. stated:

> … I do not think that describing the documents as preferred shares is conclusive as to what instrument the parties thought they were creating. In the second place, it is not what the parties call the documents that is determinative of their identity, but rather it is what the facts require the court to call them. The character of the instrument is revealed by the language creating it and the circumstances of its creation.
>
> (at 509).
>
> ...
>
> Thus, in looking at the substance of the transaction that led to the issuance of the preference shares, it appears to me that the retraction clauses were promises by Central Capital to pay fixed amounts on definite dates to the appellants. They evidenced a debt to the appellants.
>
> (at 512).

Justice Laskin specifically addressed the "substance of the relationship" at 535-36. In addition, Weiler J.A. focused on the "true nature" of the transaction or relationship:

> In order to decide whether the obligation of Central Capital to redeem the preferred shares of the appellants is a claim provable in bankruptcy, it is necessary to characterize the true nature of the transaction. The court must look to the surrounding circumstances to determine whether the true nature of the relationship is that of a shareholder who has equity in the company or whether it is that of a creditor owed a debt or liability by the company: *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, [1992] 3

> S.C.R. 558, 97 D.L.R. (4th) 385. In this case, the decision is not an easy one. Where, as here, the agreements between the parties are reflected in the articles of the corporation, it is necessary to examine them carefully to characterize the true relationship. It is not disputed that if the true nature of the relationship is that of a shareholder-equity relationship after the retraction date and at the time of the reorganization, then the appellants do not have a claim provable in bankruptcy. Consequently, they will not have a claim under the CCAA.
>
> (at 519).

[72] In *Blue Range Resource Corp. (Re)*, 2000 ABQB 4, Madam Justice Romaine found that a shareholder's claim for alleged share loss, transaction costs and cash share purchase damages was in substance an equity claim or a claim by the shareholder for a return of its investment. See also *EarthFirst Canada Inc. (Re)*, 2009 ABQB 316.

[73] In *Return on Innovation v. Gandi Innovations* , 2011 ONSC 5018, leave to appeal refused, 2012 ONCA 10, the Court was characterizing indemnity claims advanced by certain individual directors and officers against the debtor, the Gandi Group. That indemnity claim arose by reason of a claim by TA Associates Inc. against them for damages for claims relating in part to TA's US$50 million equity investment in the Gandi Group. Mr. Justice Newbould at the Ontario Superior Court concluded that TA's claim was an equity claim and that therefore, the indemnity claim was also, in substance, an equity claim.

[74] I have also been referred to *Dexior Financial Inc. (Re)*, 2011 BCSC 348. Mr. Justice Masuhara there found the claim to be an equity claim even though the shareholder had given notice of an intention to seek retraction of the shares prior to the filing. Citing *CDIC* and *Central Capital* (ONCA), the Court found that the notice did not change the original intention or substance of the claim.

(iii) The New Statutory Approach

[75] In September 2009, Parliament enacted substantial amendments to the *BIA* and *CCAA* in relation to the treatment of claims arising from equity in an insolvency proceeding.

[76] One of the principle amendments was the prohibition that the court may not sanction a plan of arrangement unless all debt claims are to be paid in full before payment of any "equity claims". Section 6(8) of the *CCAA* provides:

> (8) No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

[77] The definitions of "equity claim" and "equity interest" are found in the *CCAA*, s. 2(1):

> "equity claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (*a*) a dividend or similar payment,
>
> (*b*) a return of capital,
>
> (*c*) a redemption or retraction obligation,
>
> (*d*) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
>
> (*e*) contribution or indemnity in respect of a claim referred to in any of paragraphs (*a*) to (*d*);
>
> "equity interest" means
>
> (*a*) in the case of a company other than an income trust, a share in the company — or a warrant or option or another right to acquire a share in the company — other than one that is derived from a convertible debt[.]

[78] Section 22.1 further restricts the right of creditors having equity claims from voting on a plan of arrangement:

> 22.1 Despite subsection 22(1), creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise.

[79] Substantially these same amendments were made to the *BIA* in respect of proposal proceedings under that *Act* in ss. 2, 54(2)(d) and 60(1.7).

[80] The effect of the amendments was considered by Pepall J. (as she then was) in *Nelson Financial Group Ltd. (Re)*, 2010 ONSC 6229. In that case, the court had

no difficulty in finding that the claims of preferred shareholders for declared but unpaid dividends and requests for redemption were equity claims within the above definition. In addition, the approach of the courts in the past in looking at the substance or true nature of the claim was applied in finding that related claims for compensatory damages or amounts due on rescission were caught by the definition of "equity claim": paras. 32-34. As such, all the claims were not provable debts under the *CCAA*.

[81] The court in *Nelson Financial Group* noted that the introduction of section 6(8) in the *CCAA* provided greater certainty in the treatment to be accorded equity claims and lessened the "judicial flexibility" that previously prevailed in characterizing such claims.

[82] Accordingly, while the 2009 amendments did represent in part a codification of the previous case law concerning equity claims, it also represented a more concrete definition of "equity claims" and by such definition a broadening and more expansive definition of such claims: *Sino-Forest Corporation* (ONCA) at paras. 24, 34-60. Parliament has now clearly cast the net widely in terms of the broad definition of equity claims such that claims that might have previously escaped such characterization will now be caught by the *CCAA*.

[83] The claim of the Prestons is set out in their Statement of Claim. The claim is for the return of their capital investment under the redemption rights of the preferred shares. Their claim also included a claim to unpaid dividends, whether by cash payment or the issuance of other shares, being Class E common shares. It is clear that their claims, as evidenced by the Statement of Claim, fall within the definition of "equity claim" in subparas. (a)-(c).

[84] The Prestons do not dispute that their claim, as described and but for one qualification, would fall within the definition. They contend, however, that by reason of their obtaining default judgment against Gallowai, they have transformed their equity claim into a debt claim that is a provable claim in the *CCAA* proceeding.

(iv) The Effect of the Judgment

[85] The 2009 amendments have not affected the ability of the court to continue to analyze the *substance* of the claims, albeit in the context of the expanded definition of "equity claim". This is evident from the approach of the court in *Nelson Financial Group* at paras. 28 and 34.

[86] In *Sino-Forest Corporation*, the court found that certain Shareholder Claims for damages claimed in a class action lawsuit clearly fell within the definition of "equity claims": ONSC at para. 84. Further, certain Related Indemnity Claims were also advanced against the estate by the auditors who were named in the class action lawsuit. These auditors also faced claims for damages relating to their role in what were said to be misrepresentations in the financial statements that led to the loss of equity by the class members. Again, consistent with the historical approach of the courts, Morawetz J. focused on the "substance" of the claim: para. 85. He stated:

> [79] The plain language in the definition of "equity claim" does not focus on the identity of the claimant. Rather, it focuses on the nature of the claim. In this case, it seems clear that the Shareholder Claims led to the Related Indemnity Claims. Put another way, the inescapable conclusion is that the Related Indemnity Claims are being used to recover an equity investment.
>
> [80] The plain language of the CCAA dictates the outcome, namely, that the Shareholder Claims and the Related Indemnity Claims constitute "equity claims" within the meaning of the CCAA. This conclusion is consistent with the trend towards an expansive interpretation of the definition of "equity claims" to achieve the purpose of the CCAA.
>
> …
>
> [82] It would be totally inconsistent to arrive at a conclusion that would enable either the auditors or the Underwriters, through a claim for indemnification, to be treated as creditors when the underlying actions of the shareholders cannot achieve the same status. To hold otherwise would indeed provide an indirect remedy where a direct remedy is not available.

The Court of Appeal upheld this approach: *Sino-Forest Corporation* (ONCA) at paras. 37, 58.

[87] I would note in this regard that the Claims Process Order expressly provided:

> THIS COURT ORDERS that the categorization of Claims into Trade Claims, non-voting Shares, and Voting Shares does not in any way set classes or categories for the purposes of priority or voting on a restructuring plan issued by the Creditors and shall not prejudice any party or the Petitioners from applying at a later date to set such classes or priorities in connection with voting on a plan;

[88] The Prestons argue that their obtaining of a judgment against Gallowai has resulted in a replacement or transformation of their equity claim with a debt claim.

[89] The Prestons place considerable reliance on the decision in *I. Waxman & Sons Ltd. (Re)*, [2008] 89 O.R. (3d) 427 (S.C.), 40 C.B.R. (5th) 307, which was decided prior to the 2009 amendments to the *CCAA*. In that case, Morris sued I. Waxman & Sons Limited ("IWS") for lost profits, profit diversions and improper distributions for bonuses paid. He obtained judgment against IWS and asserted that claim in the later bankruptcy proceedings.

[90] The court began by noting that Morris' claim was not for his share of his current equity in IWS, but was, in substance, a claim related to dividends and diverted profits by way of bonuses. Justice Pepall found that the judgment was a debt claim:

> [24] There is support in the case law for the proposition that equity may become debt. For example, declared dividends are treated as constituting a debt that is provable in bankruptcy. As Laskin J.A. stated in *Central Capital Corp. (Re)*, "It seems to me that these appellants must be either shareholders or creditors. Except for declared dividends, they cannot be both." And later, "Moreover, as Justice Finlayson points out in his reasons, courts have always accepted the proposition that when a dividend is declared, it is a debt on which each shareholder can sue the corporation." Similarly, in that same decision, Weiler J.A. stated, "As I understand it, counsel does not question that when a dividend has been lawfully declared by a corporation, it is a debt of the corporation and each shareholder is entitled to sue the corporation for his [portion]: see *Fraser and Stewart*, supra, at p. 220 for a list of authorities." In *East Chilliwack Fruit Growers Co-operative (Re)*, the B.C. Court of Appeal held that an agricultural co-operative member who had exercised a right of redemption and remained only to be paid was an unsecured creditor with a provable debt. Declared bonuses may also sometimes constitute debt: *Stuart v. Hamilton Jockey Club* [footnotes omitted].
>
> [25] Secondly, the claims advanced by Morris are judgment debts. As stated by Weiler J.A. in *Central Capital*, ". . . in order to be a provable claim within the meaning of s.121 of the BIA, the claim must be one recoverable by legal process: *Farm Credit Corp. v. Holowach (Trustee of)*." Clearly a

> judgment constitutes a claim recoverable by legal process. By virtue of the judgment, the money award becomes debt and it is properly the subject of a proof of claim in bankruptcy. In this regard, the facts in this case are unlike those in *Re Blue Range Resource Corp. (Re),* or *National Bank of Canada v. Merit Energy Ltd.* Those cases involved causes of action that had been asserted in court proceedings, but in neither case had judgment been rendered [footnotes omitted].

[91] In my view, *Waxman* is of little assistance to the Prestons.

[92] Firstly, the facts are distinguishable by reason of the fact that the Preston Claim is for recovery of their capital or equity, rather than simply a return on capital as was the case in *Waxman*. I would note that the Preston default judgment obtained in 2010 does include the dividend interest on the preferred shares. What is somewhat anomalous is that this was claimed in the alternative to the issuance of the Class E common shares. Even so, the Prestons in their Statement of Claim did advance a claim for 2,102 Class E common shares and continue to do so by their Proof of Claim, all consistent with what the petitioners had ascribed to them in the Creditor List. It is not clear to me how they can advance both claims.

[93] Secondly, in para. 24 of *Waxman*, the Court focused on the prevailing authority at the time prior to the amendments by which declared dividends were considered debt as opposed to equity. At present, the 2009 amendments make clear that this type of claim now clearly falls within the definition of “equity claim” in subpara. (a): *CCAA*, s.2(1).

[94] With respect to the comments of the Court in *Waxman*, para. 25, I agree with CuVeras that the Court was simply observing that a judgment debt will normally satisfy the requirements of the claim being recoverable by legal process, one of the requirements of a “provable claim”, as noted above. These comments do nothing more than note the obvious - that in ordinary circumstances, a judgment is a claim recoverable by legal process. I do not interpret these comments as obviating an analysis of the true nature of a claim, whether represented by a judgment or not.

[95] Accordingly, I do not view *Waxman* as standing for the proposition advanced by the Prestons, namely that a judgment transforms an equity claim into a debt claim

such that no further analysis or characterization by the court is necessary. This would have applied even before the enactment of the 2009 amendments, but certainly is more evident now given the expansive definition now contained in the *CCAA*.

[96] Indeed, the later comments of Justice Pepall in *Nelson Financial Group* suggest that she only decided in *Waxman* that by reason of a judgment, an equity claim *may* become debt:

> [32] The substance of the arrangement between the preferred shareholders and Nelson was a relationship based on equity and not debt. Having said that, as I observed in *I. Waxman & Sons.* there is support in the case law for the proposition that equity may become debt. For instance, in that case, I held that a judgment obtained at the suit of a shareholder constituted debt. An analysis of the nature of the claims is therefore required. If the claims fall within the parameters of section 2 of the *CCAA*, clearly they are to be treated as equity claims and not as debt claims [footnotes omitted].

[97] The Court in *Dexior Financial* at para. 16 commented on *Waxman* but those comments were clearly *obiter* as no judgment had been obtained in that case. See also *EarthFirst Canada* at para. 4.

[98] At its core, the issue before the court is a narrow one - namely, whether a shareholder, having an equity claim but who obtains a judgment before the filing, has become a debt claimant rather than an equity claimant for the purposes of the insolvency proceeding? In my view, they do not, for the reasons below.

[99] In light of the dearth of authority on the issue, I consider that the court must start from first principles.

[100] I return to the comments in *Century Services* regarding the remedial purposes of the *CCAA* and the broad and flexible authority of this court to facilitate a restructuring that is fair, reasonable and equitable in accordance with either the express will of Parliament, as specifically dictated in the *CCAA*, or as might be reasonably interpreted as falling within those broad purposes.

[101] At its core, the policy objectives of the *CCAA* are a fair and efficient resolution of competing claims in a situation (insolvency) where all obligations or expectations cannot be fulfilled. What is "fair" is a flexible or uncertain concept and needless to say, what is fair will likely be differently interpreted depending on which stakeholder you ask. Nevertheless, Parliament has clearly signalled that the policy objectives continue to be that equity will take a back seat in terms of any recovery where there are outstanding debt claims. This was so before September 2009 and is even more decidedly so now, given the express and expansive statutory treatment of equity claims that now applies.

[102] In my view, the characterization of claims by the court continues to have an important role in fulfilling that purpose. I have already outlined the considerable authority from Canadian courts in respect of such claims, both pre- and post-amendments. Particularly, the court continues to have a role in applying these new equity claims provisions by considering the true nature or substance of those claims. In many cases, the matter is now considerably clearer given the definition of "equity claims". What is most important, however, is that form will still not trump substance in the consideration of this issue.

[103] As was noted by counsel for CuVeras, the obtaining of a judgment does not necessarily mean that it will be recognized as a debt for the purpose of an insolvency proceeding. There are many provisions of the *BIA* and *CCAA* which allow for the challenge of certain pre-filing transactions or events that may be the basis for supposed rights in the proceeding. For example, the payment of a dividend and redemption of shares may be attacked (*BIA*, s. 101). Another example is that either the granting of a judgment against the debtor or payment of monies such as redemption amounts that resulted in a preference being obtained may be challenged (*BIA*, s. 95). Both of these provisions apply in a *CCAA* proceeding: *CCAA*, s 36.1.

[104] These types of provisions reflect the policy choices of Parliament in terms of allowing for the recovery of assets transferred away from the debtor even before the filing so that those assets are brought back into the estate for the benefit of the

entire stakeholder group to be distributed in accordance with the legislation. Similarly, some established rights may be challenged in certain circumstances (such as by way of the preference provisions).

[105] In the same manner, the new equity provisions in the *CCAA* reinforce that it remains an important policy objective that equity claims be subordinated to debt claims. In *Sino-Forest Corporation*, the Court of Appeal focused on the purpose of the 2009 amendments and stated:

> [56] In our view, in enacting s. 6(8) of the CCAA, Parliament intended that a monetary loss suffered by a shareholder (or other holder of an equity interest) in respect of his or her equity interest not diminish the assets of the debtor available to general creditors in a restructuring. If a shareholder sues auditors and underwriters in respect of his or her loss, in addition to the debtor, and the auditors or underwriters assert claims of contribution or indemnity against the debtor, the assets of the debtor available to general creditors would be diminished by the amount of the claims for contribution and indemnity.

[106] This same recognition of the sound policy objectives of insolvency legislation was noted by Laskin J.A. in *Central Capital* (ONCA). He commented at 546 that "[p]ermitting preferred shareholders to be turned into creditors by endowing their shares with retraction rights runs contrary to this policy of creditor protection."

[107] I see no principled basis upon which a different approach should be taken in respect of an equity claimant who has had the foresight, energy or just plain luck to seek and obtain a judgment prior to the filing date.

[108] Some arguments were advanced by CuVeras and the Prestons as to the timing of the judgment. Indeed, the Preston judgment was obtained well in advance of the filing, by some six months. The Prestons cite *Blue Range* at para. 38 in respect of the importance of timing. However, the timing issue there was the filing of the insolvency proceeding, not the granting of a judgment. I agree that the filing of the proceeding is a significant crystallizing event, however, what is important in this case is the ability of the court to analyze the true nature of the claim. Further, whether a judgment is obtained on the eve of the filing or even years before, I consider that it is a distinction without a difference in terms of the court's role in

ensuring that a proper characterizing of the claim has taken place in accordance with the *CCAA*.

[109] The fact remains that there are thousands of other preferred shareholders holding shares in Bul River and Gallowai whose claims are in essence the same - namely, for a return of their capital and the promised return on that capital (and perhaps other damage claims). The evidence indicates that many of them had also made demand for a return of their preferred share investments and their return on capital well before the filing date. Those claims are clearly equity claims. From the perspective of the policy objective of treating similar claims in a similar fashion (i.e., fairness), it makes little sense to me that a similarly situated preferred shareholder without a judgment should be treated differently than one who does.

[110] Nor does it accord with the policy objectives particularly identified in s. 6(8) of the *CCAA* that by the simple mechanism of obtaining a judgment an equity claimant should be elevated to a debt claimant which would inevitably diminish the recovery of other "true" debt claimants.

[111] The Prestons argue that this will open the floodgates to an endless analysis of claims reduced to judgments resulting in increased cost and inefficiencies in these types of proceedings. I see no merit in this submission given that this decision relates to only equity claims and by no stretch of the imagination has the previous litigation on the point overwhelmed the court system across Canada. In any event, if that is the will of Parliament, then there is little ability in this court to take a different approach.

[112] The courts have not been hesitant in preventing claimants from recharacterizing their claims such that an equity claim is indirectly advanced where no direct claim could be made: *Sino-Forest Corporation*, ONSC at para. 84 (although the Court of Appeal preferred to express the same sentiment in terms of the purpose of the *CCAA*). In *Return on Innovation*, Newbould J. stated, consistent with the "substance over form" approach that the court's decision will not be driven by the form of the legal action:

> [59] The Claimants assert that the claim for US $50 million by TA Associates cannot be an equity claim because it is based on breaches of contract, torts and equity. I do not see that as being the deciding factor. TA Associates seeks the return of its US $50 million equity investment because of various wrongdoings alleged against the Claimants and the fact that the claim is based on these causes of action does not make it any less a claim in equity. The legal tools that are used [are] not the important thing. It is the fact that they are being used to recover an equity investment that is important.

[113] Similarly, in addition to the "legal tools" not being determinative, neither are the legal *forms* of recovery determinative, such as the obtaining of a judgment.

[114] In summary, the *CCAA* policy objectives in relation to equity claims are clear. In my view, those objectives are best achieved by the continued approach of the court, both pre- and post-*CCAA* amendments, to consider the substance or true nature of the claim. This accords with the ongoing supervisory jurisdiction of the court to exercise its statutory discretion to achieve the purposes of the *CCAA*. In particular, the court's fundamental role is to facilitate a restructuring that is fair and reasonable to all stakeholders in accordance with the now very clearly stated objective of allowing recovery to debt claimants before any recovery of equity claims. Section 6(8) reflects that the court has no ability to proceed otherwise.

[115] Within those broad objectives, in my view, it is of no importance that prior to the court filing, a claimant with an equity claim has obtained a judgment. That judgment still, in substance, reflects a recovery of that equity claim and therefore, the claim comes within the broad and expansive definition in the *CCAA*. Accordingly, for the purposes of the *CCAA*, that claim or judgment must still, of necessity, bear that characterization in terms of any recovery sought within this proceeding. I conclude that any contrary interpretation, such as advanced by the Prestons, would result in the clear policy objectives under the *CCAA* being defeated.

[116] Nor I do not accept that, as argued by the Prestons, applying this characterization amounts to a collateral attack or an "undoing" of the judgment from the Alberta court. As noted by CuVeras, the obtaining of a judgment by a creditor does not mean that insolvency laws do not apply to it. Judgments are affected by insolvency proceedings all the time. Recoveries of judgments are stayed by such

proceedings and as stated above, they can be attacked as fraudulent preferences. All that results from my conclusions is that notwithstanding the granting of the judgment, within these *CCAA* proceedings, the judgment is to be characterized in accordance with the true nature of the underlying claim, which is an equity claim.

[117] For the above reasons, I conclude that the Preston Claim is an equity claim within the meaning of the *CCAA*.

(b) The Stafford Claim

[118] The Stafford Claim is advanced as a debt claim in these proceedings. That position is disputed by CuVeras who contends that, in fact, it is a claim owed by Stanfield personally and not by either Bul River or Gallowai such that it cannot be advanced in this *CCAA* proceeding.

(i) The Proof of Claim

[119] The Creditor List referenced Mr. Stafford as holding Class B common shares (3,340), Class D preferred shares (4,200) and Class E preferred shares (17,548). He therefore received a Claims Package from the petitioners.

[120] Mr. Stafford took no issue with the shareholdings alleged to be held by him in accordance with the Creditor List. However, on October 14, 2011, a Notice of Dispute and Proof of Claim were submitted on behalf of Mr. Stafford. This was done by Carol Morrison, who was exercising a power of attorney for Mr. Stafford by reason of his mental and physical incapacity that occurred at least as early as November 2010.

[121] The Notice of Dispute refers to “claim not listed” as the “reason for dispute”. The Proof of Claim submitted by Mr. Stafford notes the “type of claim” as “other – loan and accrued interest 50% Bul River Mineral Corp. and 50% Gallowai Metal Mining Corp.” The Stafford Claim submitted is for outstanding principal and interest under a loan in the total amount of $2,587,174.

[122] The supporting documentation submitted for Mr. Stafford includes a copy of a loan agreement between Stanfield in his personal capacity, as borrower, and Mr. Stafford, as lender, dated June 12, 1990, 21 years before the CCAA filing (the "Stafford Loan Agreement"). The Stafford Loan Agreement references a loan in the principal amount of $150,000, accruing interest in the amount of 20% per annum "on the Principal", calculated yearly and not in advance.

[123] Pursuant to the terms of the Stafford Loan Agreement, Stanfield borrowed these funds for the purpose of "investing the funds in the costs of the ongoing research and development of a Process" with "Process" being defined as a "new improved method or process for extracting precious metals from ore". Paragraphs 6 and 8 of the Stafford Loan Agreement provided for a bonus payable to Mr. Stafford equal to the amount of the Principal, if the "Process" proved successful (as declared by an independent metallurgical consultant). As CuVeras submits, on its face, this was not a loan directly related to the mine or the petitioners.

(ii) Dealings in Respect of the Stafford Loan Agreement

[124] For obvious reasons, the death of Ross Stanfield and the incapacity of Mr. Stafford result in a situation where no individual is in a position to shed light on the intentions of the parties in relation to this loan. Mr. Hewison is similarly unable to provide any evidence about the loan, save for referring to such documents as have been found in relation to this loan. Those documents do provide some indication as to the how Stanfield, Bul River and Gallowai addressed this loan up to the time of the *CCAA* filing.

[125] There are two resolutions of the directors of Bul River, dated October 1994 and February 1996 respectively, that are essentially the same. Both refer to the "need of major amounts of additional financing" and authorize Stanfield to negotiate, on behalf of Bul River, potential sources of debt or equity financing, to settle the terms of the financing, and to sign, seal and deliver any agreements necessary to secure funding required by the company. I agree that these resolutions on their face clearly do not authorize Stanfield to act as an agent for Bul River. They merely

authorize him to act directly in the name of the company with the company as principal in respect to those transactions. These resolutions also do not reference any loan by Mr. Stafford to Stanfield made years before in June 1990.

[126] Bul River also appears to have prepared a schedule of loan payments as of December 31, 2006. That schedule shows payment of interest to Mr. Stafford by Stanfield personally from June 1995 to September 1998 totalling approximately $183,000. In 1999 and 2000, Gallowai appears to have made interest payments of $40,000 and from that time forward, some person (unidentified) made interest payments of $25,000 for 2001 and 2002. From 2004 to 2006, it appears that Bul River made interest payments of $22,500 and principal payments of $26,000 to Mr. Stafford. Mr. Stafford's own calculations show further payments of interest from 2007 to 2009 totalling $58,000.

[127] Accordingly, in respect of his $150,000 loan, as of 2009, Mr. Stafford had received $328,100 in interest payments and $26,000 in principal payments for a total recovery of $354,100.

[128] Leaving aside the interest and principal payments referred to above, the involvement of Bul River and Gallowai in respect of the Stafford Loan Agreement arose, from a corporate perspective, in 2003. At that time, various resolutions were passed by the directors of Bul River. Mr. Stafford places great reliance on these resolutions and as will become apparent from the discussion below, the issue largely turns on the legal effect of these resolutions. As such, I will describe the resolutions in some detail.

[129] The first resolution is dated May 13, 2003. It provides:

> WHEREAS:
>
> A. Loans, loan repayments and principal and interest payments which were property for the benefit of, or were the responsibility of, the Company have for some years been done, as a matter of convenience, in the name of the Company's President, [Stanfield] - and as a result debit and credit entries have improperly been posted to Stanfield's Shareholder Loan Account.
>
> B. Stanfield has requested that the situation described above be corrected…

> C. The Companies' accountant has examined the financial records and has verified that the said situation has occurred with respect to the Company as well as Gallowai…
>
> D. Management has proposed, based on professional advice, that for convenience and simplicity the various Loan Accounts involving Stanfield, the Company and the Other Companies be consolidated in the books of the Company.
>
> …
>
> NOW THEREFORE, IT IS RESOLVED:
>
> 1. THAT the Loan Accounts and payments referred to above be recognized as solely the responsibility of the Company and it be confirmed that Stanfield was, in being named in the transactions, acting solely on behalf of the Company and that he had no personal, legal or beneficial interest in, or any liabilities as a result of, any of the transactions.
>
> 2. THAT the Agreement dated this May 13, 2003 between the Company, Stanfield and the Other Companies be approved and that Stanfield or any other officer or director of the Company be authorized to sign and deliver it on behalf of the Company.
>
> 3. THAT the Company assume the obligations of the Other Companies to Stanfield pursuant to the shareholder account in their records, to be offset by inter-company accounts whereby each of the Other Companies will be indebted to the Company for the amount of shareholders accounts assumed by the Company.

[130] The second resolution of Bul River is dated October 20, 2003 and relates to the May 2003 resolution. The resolution references that Stanfield is having difficulty providing full documentary verification and back-up for his expenditures for which he was requesting reimbursement. In addition, the preamble to the resolution states in part:

> D. Acceptance of liability to Stanfield at this date poses some special problems due to the fact that some of the disbursements that he has requested to be reimbursed for precede the last date that the financial statements of the company were audited – and such statements did not include the expenditures.

Concern was expressed whether or not the acceptance of these responsibilities would be acceptable to Bul River's auditors. The resolution authorizes the engagement of the auditors for the purpose of conducting a special audit of the expenditures made by Stanfield. There is no evidence as to the result of that special audit or if it even took place.

[131] The third resolution of Bul River is dated November 30, 2003 and is of particular significance. It reads as follows:

> WHEREAS:
>
> A. Ross Stanfield …has submitted various claims for recognition of corporate liabilities to third parties ... as shareholder's loans for transactions undertaken as agent on behalf of the Company, Gallowai … to finance the exploration of the British Columbia properties owned by the Companies ("Properties").
>
> B. Stanfield and the Companies signed an Agreement dated May 13, 2003 recognizing the fact that Stanfield has acted as agent on behalf of the Companies since 1972 and had personally undertaken a variety of transactions as agent for the Companies to finance the exploration of the Properties.
>
> C. Stanfield has submitted the following claims pursuant to the Agreement for the Director's consideration and approval.
>
> 1. Exploration Loans
>
> These loans were negotiated between 1983 and 2002 personally by Stanfield, as the agent of the Company, and all funds were advanced to the Companies as shareholders loans from him. Payments were made on the loans with his own personal funds or shareholdings. The Directors were provided with a summary of individual loans and accrued interest for review. Files have been prepared for corporate record keeping purposes that include the documentation and amortization schedules supporting each loan.
>
> Balances as at December 31, 2002
>
> | | |
> |---|---|
> | Loan principal | $1,886,413 |
> | Accrued interest | $6,281,004 |
>
> …
>
> **NOW THEREFORE**, the undersigned acting as a group excluding … [Stanfield], RESOLVE:
>
> 1. THAT the loans, accrued interest and share subscriptions detailed in paragraph C.1 above, negotiated by Stanfield as agent on behalf of the Companies, be accepted as liabilities of the Companies.
>
> …
>
> 3. THAT the resolution passed by the full Board dated May 13, 2003 that the Company accept all of the above described liabilities on behalf of the other Companies – to be offset by inter-company accounts whereby each of the other Companies will be indebted to the Company for the amounts assumed by the Company – be further approved and ratified.

[132] It should be noted that the agreement between Stanfield and Bul River (and perhaps others) dated May 13, 2003 has not been located. Nor have any similar resolutions from the directors of Gallowai been found.

[133] In addition, no one has been able to locate a copy of the summary of the loans as of December 2002 referred to in paragraph C.1 of the November 2003 resolution. Mr. Hewison refers in his evidence to a spreadsheet in the name of Bul River referencing "Mine Development Loans" for the year ended December 2003 which indicates a loan from Mr. Stafford of $150,000 with accrued interest of $899,236.39. The total interest figure for all loans is slightly different (lower) than the interest amount referenced in the November 2003 resolution which was as of December 31, 2002. In any event, CuVeras does not dispute that Mr. Stafford would likely have been on the list referred to in the November 2003 resolution.

[134] No audited financial statements have been produced pre-2003, as might have been amended arising from the special audit authorized in October 2003.

[135] Also in evidence are various letters from Bul River to Mr. Stafford concerning these loans.

[136] On April 23, 2007, a letter was sent to Mr. Stafford's accountant enclosing various amended 2006 T5 (Statement of Investment Income) forms or slips that were apparently issued to Mr. Stafford by Gallowai and Bul River, each as to 50% of interest paid or payable pursuant to the Stafford Loan Agreement. The letter indicates that as of 2006, the amount of such interest was just over $1.5 million (which included the $150,000 bonus amount supposedly due pursuant to the Stafford Loan Agreement).

[137] On March 6, 2008, Mr. Stafford received correspondence from Bul River's controller concerning the 2006 T5s slips from Bul River and Gallowai. Later letters from the controller dated April 2, 2008, February 12, 2009 and January 19, 2010 refer to T5 slips being issued by Bul River and Gallowai for 2007, 2008 and 2009 relating to accrued interest on the Stafford Loan Agreement. Finally, T5 slips for 2010 appear to have been issued by Bul River and Gallowai for that taxation year.

[138] There is no evidence that Mr. Stafford knew anything about the 2003 resolutions by Bul River. It does appear to be the case that he began receiving

interest payments from Gallowai in 1999 and these would continue together with the payment of some principal by either Gallowai or Bul River to 2009. Bul River would also later send Mr. Stafford, commencing in 2007 and continuing to 2010, certain details or statements relating to the loan and the T5 slips.

(iii) Legal Basis for the Stafford Claim

[139] For the reasons set out below, CuVeras submits that the Stafford Claim is not a debt claim against Bul River and Gallowai and ought to be expunged from the Creditor List. CuVeras argues that Mr. Stafford cannot satisfy the onus placed upon him to prove his claim against those petitioners.

[140] At the outset, it is clear that Mr. Stafford advanced his loan to Stanfield personally, and not to either Bul River or Gallowai. The 2003 resolutions confirm that such was the case and, indeed, the amounts were noted in the books of Bul River and Gallowai as shareholder loans owing to Stanfield personally in that respect.

[141] CuVeras made substantial arguments on the later involvement of Bul River and Gallowai in terms of whether those petitioners became the principal obligants under the Stafford Loan Agreement. These arguments related to whether or not there had been a valid assignment of the Stafford Loan Agreement from Stanfield to Bul River and Gallowai. While Mr. Stafford agreed with these submissions, it is helpful to set out these issues and arguments in order to put in focus the later arguments of Mr. Stafford (which are contested by CuVeras).

[142] I agree that there is no basis upon which Mr. Stafford can contend that Stanfield assigned the Stafford Loan Agreement to Bul River and Gallowai. There is no evidence that Gallowai agreed to anything, since the resolutions were only that of Bul River's directors.

[143] Even assuming that the November 2003 resolution was intended to effect a valid assignment of the obligations under the Stafford Loan Agreement from Stanfield to Bul River and Gallowai, it is of no legal effect in that it purports to assign the burden of Stanfield's obligations to Bul River and Gallowai. It is trite law that

neither the common law nor equity has ever permitted a debtor to unilaterally assign the burdens or obligations (as opposed to the benefits) of a contract to a third party without the consent of the creditor. Rather, in that case a novation is required: *Mills v. Triple Five Corp.* 1992 CanLII 6204 (Alta. Q. B.) at paras. 13-14, [1992] 136 A.R. 67.

[144] Novation involves the substitution of a new contract or obligation for an old one which is thereby extinguished: *Royal Bank of Canada v. Netupsky*, 1999 BCCA 561. In *Netupsky* at paras. 11-13, the court set out the essential elements that must be established to satisfy the test to establish novation:

> 1. the new debtor must assume complete liability for the debt;
>
> 2. the creditor must accept the new debtor as a principal debtor, and not merely as an agent or guarantor; and
>
> 3. the creditor must accept the new contract in full satisfaction and substitution for the old contract.

[145] Mr. Stafford bears the burden of proving novation which the Court in *Netupsky* described as a "heavy onus". Further, while the courts may look at the surrounding circumstances, including the conduct of the parties, they will not infer that a novation has occurred in the face of ambiguous evidence as to the parties' intention to effect a new agreement with the substituted party.

[146] As is noted by CuVeras, it is somewhat ironic to suppose that Mr. Stafford might have advanced this issue since he is the creditor and as noted in *Netupsky*, it is usually the "unwilling creditor" who is objecting to any suggestion of a novation. In any event, in this case there is no evidence to suggest that:

a) Mr. Stafford had any knowledge of the 2003 resolutions or was in any other way even advised by Stanfield, Bul River or Gallowai that it was intended that Bul River and Gallowai would assume the obligations under the Stafford Loan Agreement in place of Stanfield; and

b) Stanfield, Bul River, Gallowai and Mr. Stafford reached a consensus with respect to the terms upon which any purported new or substituted agreement would operate.

[147] Accordingly, it is clear, as agreed by CuVeras and Mr. Stafford, that novation did not occur such that Bul River and Gallowai assumed the obligations of Stanfield under the Stafford Loan Agreement with the consensus of Mr. Stafford. In addition, no privity of contract arose simply by reason of later payments to Mr. Stafford or issuance of T5 slips by Bul River and Gallowai. That Mr. Stafford was not directly involved in any such new contractual arrangements and that he only later "assumed" that Bul River and Gallowai were involved is made evident by his own loan summary attached to his Proof of Claim:

> Commencing in 2006, T5 slips were issued by Bul River Mineral Corporation and Gallowai Metal Mining Corporation (50% each). Assumption is therefore that ½ of Grand Total is receivable from each.
>
> [Emphasis added].

[148] Nor is there any suggestion that Bul River or Gallowai provided a guarantee of the Stafford Loan Agreement to Mr. Stafford. Finally, Mr. Stafford does not argue that Bul River and Gallowai are somehow estopped from denying that they are debtors of Mr. Stafford, particularly by reason of the interest and principal payments made by them and the T5 slips prepared by them which were then forwarded to Mr. Stafford.

[149] Having confirmed the agreement of CuVeras and Mr. Stafford on the above issues, I turn to Mr. Stafford's position, which is solely rooted in agency:

> The corporate minutes of Bul River Mineral Corporation confirm that the actions of Ross Hale Stanfield were as agent for the company and associated companies and confirmed by resolution to accept liability of agreements signed by Stanfield as legitimate debts of a company and acted on it accordingly[.]

[150] Essentially, Mr. Stafford's argument is that Stanfield was retroactively appointed as the agent of Bul River and Gallowai by reason of the November 2003 resolution such that he had the express or implied authority to bind Bul River and

Gallowai at the time of the loan. He relies in particular on s. 193(2) and (4) of the *Business Corporations Act*, S.B.C. 2002, c. 57:

> 193 (2) A contract that, if made between individuals, would, by law, be required to be in writing and signed by the parties to be charged, may be made for a company in writing signed by a person acting under the express or implied authority of the company and may, in the same manner, be varied or discharged.
>
> …
>
> (4) A contract made according to this section is effectual in law and binds the company and all other parties to it.

[151] It seems to be common ground that Stanfield was not acting as the agent of Bul River and Gallowai in 1990 when the loan was made. The Stafford Loan Agreement does not reference Stanfield acting as an agent and the Proof of Claim does not allege an agency relationship at the time of the Stafford Loan Agreement. Nor was Stanfield acting as the agent of Bul River and Gallowai during the ensuing 13 years when the loan was being administered. The allegation is that changes only occurred in 2003 when Stanfield decided he wanted to be reimbursed by Bul River and Gallowai for certain loans he had earlier made.

[152] I was referred to only one authority on the agency issue by CuVeras, being *Spidell v. LaHave Equipment Ltd.*, 2014 NSSC 255.

[153] In *Spidell*, LaHave Equipment Ltd. was a dealer for Case Canada Limited. The plaintiff Spidell purchased a Case Canada excavator from LeHave which was financed by Case Credit Limited. Spidell alleged that employees of LaHave made representations to him about the performance of the equipment. Spidell believed LaHave was a representative or agent or dealer for Case Canada. Spidell did not make the required payments to Case Credit and the equipment was repossessed. Spidell sued LaHave claiming damages for alleged misrepresentations. LaHave defended the action but subsequently went into bankruptcy. Only then did Spidell amend his pleading to add Case Credit and Case Canada as defendants, claiming LaHave was their agent. The issue on the summary trial was whether LaHave was in fact the agent of the Case companies.

[154] Mr. Justice Coughlan reviewed the law of agency, as follows:

> [21] In *Halsbury's Laws of Canada First Edition,* "Agency" paragraph HAY-2 the three essential ingredients of an agency relationship are:
>
> "1. The consent of both the principal and the agent.
>
> 2. Authority given to the agent by the principal, allowing the former to affect the latter's legal position.
>
> 3. The principal's control of the agent's actions."
>
> And at Agency paragraph HAY -11 the manner in which an agency relationship may be created are set out:
>
> "1. the express or implied consent of principal and agent,
>
> 2. by implication of law from the conduct or situation of the parties or from the necessities of the case,
>
> 3. by subsequent ratification by the principal of the agent's act done on the principal's behalf, whether the person doing the act was an agent exceeding his authority or was a person having no authority to act for the principal at all,
>
> 4. by estoppel, or
>
> 5. by operation of the principles of law."
>
> [Emphasis added].

[155] Mr. Stafford relies in particular on the creation of agency by ratification as referred to above. Justice Coughlan said this about agency by ratification:

> [25] The conditions for an agency by ratification to be established were set out in *Halsbury's Laws of Canada, supra*, at Agency HAY-22 as follows:
>
> "**Three Conditions**. Actions by a principal after the agent has purported to act on the principal's behalf may amount to creation of agency by ratification. For this to occur, three conditions must be satisfied. First, the agent whose act is sought to be ratified must have purported to act for the principal; second, at the time the act was done the agent must have had a competent principal; and third, at the time of the ratification the principal must be legally capable of doing the act himself.["]

[156] The key consideration from the above quote is the first requirement. In this case, there is no evidence that Stanfield "purported to act" for Bul River and Gallowai as principals in 1990 when he entered into the Stafford Loan Agreement. In fact, the evidence is to the contrary in that he acted in his personal capacity and not as agent.

[157] I agree with CuVeras that agency by ratification assumes that there exists a relationship (even though perhaps mistaken) between the principal and agent at the time of the transaction which must later be ratified. One example is as noted in the *Halsbury's* quote above, namely where the agent exceeded his or his authority but later the unauthorized transaction is ratified or adopted by the principal. That is not what occurred in this case. Ratification of an agent's actions in that case cannot occur when no agency relationship existed in the first place. The second example of ratification described in *Halsbury's* (where the person had no authority to act but their actions were later ratified) still requires that the actions be done by the agent "on the principal's behalf" in purported furtherance of an agency relationship.

[158] Accordingly, the concept of ratification by Bul River and Gallowai of Stanfield's actions concerning the Stafford Loan Agreement as their agent has no application in this case.

[159] What occurred in this case is that many years later, in 2003, Stanfield, Bul River and Gallowai agreed that the companies would take over responsibility for payment of the Stafford Loan Agreement in place of Stanfield. But those arrangements were only between Bul River, Gallowai and Stanfield and not Mr. Stafford.

[160] Accordingly, we start from the proposition that there was no agency relationship between Stanfield and Bul River and Gallowai in 1990. The only parties to the Stafford Loan Agreement are Stanfield and Mr. Stafford.

[161] The only evidence suggesting any link between Mr. Stafford and Bul River and Gallowai arise from the fact that, commencing in April 2007, Mr. Stafford began to receive T5 slips from them. Payments were also made by Bul River and Gallowai commencing in 1999. Mr. Stafford argues that by reason of such actions, Bul River and Gallowai treated the Stafford Loan Agreement as their debt since they could not have issued T5 slips for someone else's debt. The 2003 resolutions are, of course, an internal document of Bul River but do indicate that Bul River at least intended to accept the Stafford Loan Agreement as its obligation. The basis upon which Bul

River was able to accept this obligation on behalf of Gallowai is unclear and not substantiated.

[162] Mr. Stafford argues that these events confirm that Bul River and Gallowai had assumed the obligations of Stanfield. But this argument brings us back to the legal bases for any liability on the part of Bul River and Gallowai that CuVeras raised and I discussed above (assignment, novation, guarantee and estoppel) and which arguments Mr. Stafford agreed did not apply.

[163] I agree with the submissions of CuVeras that these later actions of Bul River and Gallowai evidence an intention on the part of Bul River (and perhaps Gallowai) to take over or assume payment of the obligations of Stanfield under the Stafford Loan Agreement. In that sense, and without a novation, in substance these arrangements amount to Bul River and Gallowai agreeing to indemnify Stanfield in respect of his obligations to pay the Stafford Loan Agreement amounts and nothing more.

[164] I conclude that Mr. Stafford has not met the onus of proving that the amounts under the Stafford Loan Agreement are obligations or "provable debts" of Bul River and Gallowai.

[165] Both CuVeras and Mr. Stafford made submissions concerning the issue as to whether the Stafford Loan Agreement provided for compound interest or not. In light of my conclusions above, it is not necessary to address that issue.

Conclusion

[166] In accordance with the above reasons, the Court declares that:

a) the Preston Claim is an equity claim for the purposes of this *CCAA* proceeding; and

b) the Stafford Claim is not a debt claim as against Bul River and Gallowai. It follows that the Creditor List should be amended accordingly and that

> Mr. Stafford is not entitled to vote on or receive any distribution under any plan of arrangement as may subsequently be filed by those petitioners.

[167] If any party is seeking costs, then written submissions should be delivered to the court and the party against whom costs are sought within 30 days of delivery of these reasons. Any response shall be delivered within 15 days and any reply to that response shall be delivered with seven days of that date.

"Fitzpatrick J."

TAB 12

CV-20-00642928

Re Clover on Yonge Inc

(1) This is a motion for an Order sanctioning the Plan of Compromise and Arrangement dated November 6, 2020. ("Plan")

(2) The Plan was approved on December 15, 2020 by the requisite Statutory Majorities of affected creditors with voting claims in each of the Plan's two classes of creditors. 96.6% of the Depositor Creditor claims voted in favour of the

Plan and 98.8% of the General Unsecured Creditor Class voted in favour of the plan.

(3) There is one unresolved Voting claim advanced by Maria Athanasoulis, which she values at $49 Million ("Maria's claim"). If this claim is accepted in the value asserted, the Plan would be defeated in the General Unsecured Creditor Class. All but $1 million of Maria's claim is a claim for a share of

profits in a number of projects, including the Clover on Yonge project.

(4) I accept the Monitor's position that with respect to the component of Maria's claim related to an alleged profit sharing agreement with respect to the Clover on Yonge project there was no prospect of any profit from that project because as of March 31, 2020, shortly after the receivership commenced, the Clover on Yonge project was forecast to generate a loss of $61 Million. As a

result because I accept that the proper date to value Maria's claim is when the receiver was appointed on March 27, 2020 There was no profit known. The closest on Gorge Project that could be shared with Maria.

⑤ Mr Dunn, on behalf of Maria, concedes there can be no profit from this project under the Pre-sale unit purchase contracts are disclaimed. I have already ordered that these contracts can only

be disclaimed if the Plan is approved.

(6) As the Monitor points out in the Supplementary Report & its 14th Report any forecast profit is entirely dependent on the restructuring of the leases of the Clover Leaf Project. I accept and adopt the Monitor's following Statement:

"It does not assist Ms. Athanasoulis to argue she is entitled to share in profit derived from a successful Plan That she would vote against and cause to fail

if she had a claim.))

(7) In my view I agree that the relevant date to calculate her profit-sharing claim is later than the secondment appointment date and that profit could be deemed from the Cloud on Yonge Project is just too remote and speculative and lacks an air of reality. I agree with the Applicants' submission that "there is no profit absent disclaimer, and no disclaimer absent the approval, sanction and

implementation of the Plan. Accordingly, if the profit component of the alleged Athanasoulis claim is allowed for negative voting purposes, it must follow that the value attributed to it is a profit expectation of $ nil, and not a profit expectation of $48 Million."

(8) The criterion I must use to determine if Maria's claim, which is a contingent claim, is to be included in the insolvency proceeding is whether the event that has

not yet accrued is too remote or speculative. For my view Maria's claim cannot be shown to be neither too remote nor speculative unless the plan is approved, sanctioned and implemented. This is the very event that Maria would defeat if her contingent profit-sharing claim of $48 Million is allowed for voting purposes.

(9) I rely on Justice Morrison's decision in Nelson Energy v. Grant Thornton, 2015 NBQB 20 at para 35 where he

Opposed the proposal trustee's decision to disallow a contingent creditor's claim for purpose of voting on a summary basis on facts that are strikingly similar to the facts in this case.

(10) Accordingly, I have concluded, for the reasons outlined above, that Mona's claim is so speculative and remote in the amount of $48 Million to be allowed for voting purposes. I will therefore not have to consider whether Mona's claim is an equity claim that should not be counted for voting purposes.

(11) With respect to the issue of whether the Plan should be sanctioned, I am satisfied that,

(a) It has been approved by the requisite statutory majority of the Applicants' non-equity creditors;

(b) There has been strict compliance with all statutory requirements and adherence to previous orders of the Court;

(c) Nothing has been done, or purported to be done

(11) that is not authorized by the CCAA; and

(d) The Plan is fair and reasonable.

(12) In conclusion, for the reasons set out above, the Plan is sanctioned by the Court in its entirety and I declare that Maria's claim cannot be valued at more than $1 Million (the wrongful dismissal portion of the claim) for voting purposes with respect to the Plan.

(12)

(13) An order shall go to this effect.

(14) I thank all counsel for their helpful submissions.

Harvey J.

January 8, 2021

TAB 13

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Dexior Financial Inc. (Re),* 2011 BCSC 348

Date: 20110322
Docket: B080055
Registry: Vancouver

IN BANKRUPTCY AND INSOLVENCY

In the Matter of the Bankruptcy of

Dexior Financial Inc.

Before: The Honourable Mr. Justice D.M. Masuhara

Reasons for Judgment
In Chambers

Counsel for Trustee in Bankruptcy:	J.I. MacLean, Q.C.
Counsel for Halltray Farms Ltd.:	G. Dabbs
Place and Date of Hearing:	Vancouver, B.C. January 31, 2011
Place and Date of Judgment:	Vancouver, B.C. March 22, 2011

Introduction

[1] Pursuant to s. 34 of the *Bankruptcy and Insolvency Act*, R.S. 1985, c. B-3 [BIA], the Trustee in Bankruptcy of Dexior Financial Inc. ("Dexior") seeks directions with respect to the validity of a number of claims received.

[2] The Trustee has received approximately 67 claims to date totalling $18,823,688. Of those claims, the Trustee says some 30 involve equity claims and the equity component totals approximately $9,375,000.

[3] The Trustee puts the equity claims into the following categories:

(a) Investors who purchased shares in Dexior and have had shares issued to them.

(b) Investors who have claimed for dividends on their shares in Dexior, in accordance with statements issued to them showing such dividends.

(c) Investors who gave a notice of redemption to Dexior but the notice period had not run out before the date of bankruptcy.

(d) Investors who made advances to an entity other than Dexior.

(e) Investors who made advances through Dexior Financial Inc. to an entity other then Dexior.

(f) Investors who bought shares but claim to have been defrauded by Dexior.

[4] Dexior filed a Notice of Intention to Make a Proposal on December 17, 2007. A Proposal was subsequently filed but voted down at the meeting of auditors on February 12, 2008. As a result, Dexior became bankrupt on February 12, 2008.

[5] The Trustee deposes that:

(a) Dexior was under the de facto control of Mr. Gerard Darmon and Mr. Mohammed Jiwani;

(b) funds raised by Dexior were invested in a series of projects or investments that were ill conceived;

(c) Dexior was never in a position to pay dividends or fund the retraction of Class J to M shares from “profits” as none of the projects ever produced any profits for Dexior; and

(d) a review of the corporate records of Dexior does not disclose any dividends of any shares having been declared by the directors.

[6] The Trustee is of the view that the above-mentioned claims should be disallowed as they are equity claims and seeks the courts direction in this regard.

Discussion

[7] The only respondent appearing at this hearing was Halltray Farms Ltd. (“Halltray”). Halltray was a holder of Class P preferred shares in Dexior. Its claim in regard to this hearing relates to its investment of $1 million in the preferred shares. It concedes that it was a shareholder and thus had an equity claim but submits that its status changed to that of an ordinary creditor when it provided its notice of intention seeking retraction of its shares and as such is eligible to participate in a distribution. The notice was provided May 10, 2007. Halltray says that although the end of the notice period applicable to its retraction notice had not run out prior to the date of Dexior filing its Notice of Intention pursuant to the *BIA* the end of its retraction notice period had run out prior to the date of the bankruptcy on February 12, 2008. The Trustee during the course of the hearing advised that Halltray was the only claimant to have delivered a retraction notice.

[8] Halltray relies primarily upon Re *East Chilliwack Agricultural Co-operative,* 58 D.L.R. (4th) 11 (B.C.C.A.) in support of its position. The facts in *East Chilliwack* are similar to those as in this case. The case involved members of the cooperative who had given written notice of their intention to withdraw. The rules of the cooperative provided that the withdrawing member would cease to be a member at the time of the notice and could elect to have his share redeemed either in equal instalments over five years or in one payment with interest at the end of five years. The cooperative subsequently made a voluntary assignment in bankruptcy. The Trustee sought directions from the court as to whether the withdrawing members could file as unsecured creditors under the then *Bankruptcy Act*.

[9] The majority in *East Chilliwack* decided that the withdrawing member having provided his notice was an unsecured creditor and not a shareholder. They focused on the fact that the withdrawing member had ceased to be a member by operation of the co-operative's memorandum of association and as such was "no longer to participate in the profits of the co-operative enterprise as a shareholder".

[10] The cases relied upon by the Trustee in respect to all of the claims identified in this proceeding are: *Re Blue Range Resource Corp.*, 2000 ABQB 4, 15 C.B.R. (4th) 169 [*Blue Range*]; *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, [1992] 3 S.C.R. 558 [*CDIC*]; *Re Central Capital Corp.* (1996), 132 D.L.R. (4th) 223 (Ont. C.A.); *National Bank of Canada v. Merit Energy Ltd.*, 2001 ABQB 583, 28 C.B.R. (4th) 228 [*Merit Energy*]; and *National Bank of Canada v. Merit Energy Ltd.*, 2002 ABCA 5, 3 W.W.R. 215.

[11] A review of the cases referred to by the Trustee indicates that the jurisprudence as it is today appears to have overtaken the majority view in *East Chilliwack*. The leading case being the Supreme Court of Canada in *CDIC*. In that case, Iaccobucci J. identified that the characterization of the transaction under review requires the determination of the intentions of the parties. In other words, to determine what the substance of the arrangement reflects. He stated at 37:

> As I see it, the fact that the transaction contains both debt and equity features does not, in itself, pose an insurmountable obstacle to characterizing the

> advance of $255 million. Instead of trying to pigeonhole the entire agreement between the Participants and CCB in one of two categories, I see nothing wrong in recognizing the arrangement for what it is, namely, one of a hybrid nature, combining elements of both debt and equity but which, in substance, reflects a debtor-creditor relationship. Financial and capital markets have been most creative in the variety of investments and securities that have been fashioned to meet the needs and interests of those who participate in those markets. It is not because an agreement has certain equity features that a court must either ignore these features as if they did not exist or characterize the transaction on the whole as an investment. There is an alternative. It is permissible, and often required, or desirable, for debt and equity to co-exist in a given financial transaction without altering the substance of the agreement. Furthermore, it does not follow that each and every aspect of such an agreement must be given the exact same weight when addressing a characterization issue. Again, it is not because there are equity features that it is necessarily an investment in capital. This is particularly true when, as here, the equity features are nothing more than supplementary to and not definitive of the essence of the transaction. When a court is searching for the substance of a particular transaction, it should not too easily be distracted by aspects which are, in reality, only incidental or [page591] secondary in nature to the main thrust of the agreement.
>
> The weight to be given to one aspect of the support agreements over another in assessing the true intention of the parties underlies the difference in opinion between the learned chambers judge and the Court of Appeal's characterization of the transaction. Wachowich J. emphasized both the fact that the recovery by the Participants of their contribution was dependent upon the income generated by CCB and the Participants' potential to share in the future success of CCB by the warrants, even after having been repaid, as evidencing that the essence of the transaction was that of a capital investment. The Court of Appeal, however, largely dismissed the relevance of the Equity Agreement because of its contingent nature and emphasized instead that the Participants were only entitled to receive from CCB the amount advanced to it and that the parties had included specific provisions in the Participation Agreement referring to debt; all of which amounted to a very strong indicium of a loan.
>
> [Emphasis Added]

[12] The dissenting opinion of Justice Craig in *East Chilliwack* appears to be in line with the views in the above quoted passage from *CDIC*. At 19, he stated:

> When a person subscribes for shares in a co-operative, he contributes his capital in varying amounts hoping that he will eventually participate in the profits by way of dividends or bonuses. I agree with the submission of counsel for the respondents that the court must look at the contributions at the time when they are made in order to ascertain their nature, that is, whether they are to be contributions to the business or whether they are to be by way of loan. Here, the appellants contributed to the capital of the business which was carried on for the joint benefit of an members of the association

> with a view to participating in the profits by way of dividends or bonuses. It would be grossly inequitable to allow these withdrawing members to compete with trade creditors in the case of a bankruptcy. I think the extract from Halsbury cited by Ritchie, J. in Sukloff is apposite in this case. [Emphasis added]

[13] The majority decision did not focus on the nature of the relationship when the shares were purchased or the substance relationship underlying the claim. The majority in *East Chilliwack* focussed on the fact that the withdrawing shareholder in the cooperative had ceased to be a member upon delivering his notice of intention to withdraw as a member. I also note that counsel for the Trustee in the instant case advises that the articles applicable to the terms of the shares held by Halltray are standard terms applicable to preferred shares and further do not say that Halltray ceases to be a shareholder upon provision of a retraction notice. Counsel for Halltray did not contest this point. Further, counsel for Halltray did not provide submissions with respect to any other aspect of the articles of Dexior applicable to the subject preferred shares which could distinguish the claim from *CDIC* or *Re Central Capital Corp.*

[14] I note as well that the preferred shares are indentified as forming part of the capital of Dexior. In Part 44 of the articles of Dexior specify that the preferred shareholders rank with other shareholders in a defined priority in the event of liquidation, dissolution or winding up of the company or other distribution of its assets among the members for the purpose of winding up its affairs, distribution of property and assets of the company. There is no suggestion that these shareholders have priority equivalent to ordinary creditors.

[15] Counsel for the Trustee also notes that *Re Central Capital Corp.* also dealt with the retraction rights in preferred shares and that the Ontario Court of Appeal in a 2-1 decision declined to follow *East Chilliwack.* I note particularly the comments of Laskin J.A. at 269 and 270 where he set out several reasons for not accepting *East Chilliwack* as follows:

> …I decline to apply *East Chilliwack* for three reasons. First, because the case was decided in 1989, the British Columbia Court of Appeal did not have the benefit of the Supreme Court of Canada's reasons in *CDIC v. CCB*,

> *supra*. In *East Chilliwack* Hutcheon J.A., writing for the majority, did not focus on what the parties intended when the member contracted with the co-operative. Instead he only considered the relationship between the member and the co-operative after the member had withdrawn. I do not think his approach is consistent with Justice Iacobucci's judgment in *CDIC v. CCB*, *supra*.
>
> Second, there are important factual differences between *East Chilliwack* and the appeals before us. Justice Weiler has referred to these factual differences in her reasons. The most important of these differences are the following: in *East Chilliwack* the rules of the association provided that a member had to withdraw from the association to trigger the right of redemption, whereas the appellants' share conditions provide that they continue to be shareholders of Central Capital until their shares are redeemed; in *East Chilliwack* the member elected to withdraw and redeem his shares when the association was solvent whereas when the appellant McCutcheon exercised his right of retraction Central Capital was insolvent; and in *East Chilliwack* Hutcheon J.A. expressly stated that he was not considering the effect of the superintendent's power to suspend payments if the financial position of the co-operative was impaired, whereas the effect of the statutory prohibition against Central Capital making payment, found in s. 36(2) of the *Canada Business Corporations Act*, is in issue in these appeals.
>
> Third, the decision in *East Chilliwack* is at odds with most of the American case-law and I favour the American approach. When a company repurchases shares by instalment and bankruptcy intervenes, the prevailing American position is that the shareholder's claim is deferred to the claims of ordinary creditors. The decision of the Fifth Circuit Court of Appeals in *Robinson v. Wangemann*, 75 F. 2d 756 (1935), is frequently cited. The facts of that case are virtually identical to the facts in *East Chilliwack*.

In my view the authorities subsequent to *East Chilliwack* lead me to conclude that in this case the claims of the respondents as described by the Trustee in paras. 3(a), (b) and (c), which include Halltray's, in respect to the preferred shares, are equity claims. As earlier noted respondent's counsel conceded that Halltray held equity claims until their notice of retraction.

[16] Counsel for Halltray points out that the circumstances of Halltray are different from those in *CDIC* and *Central Capital* in that Halltray had provided its retraction notice prior to bankruptcy whereas in the other two cases the claims arose after bankruptcy. In my view, that distinction does not assist Halltray as the notice does not change the original intention or substance of the claim. I note that there have been some recent cases in other provinces which indicate that a judgment obtained

with respect to claims such as in this case could entitle the judgment holder to have a claim equal to other claimants, see for example: *I. Waxman & Sons Limited (Re)*, (2008) 89 O.R. (3d) 427 (S.C.). However in this case no such judgment had been obtained.

[17] I further note that the recent statutory changes to the *BIA*, which are not applicable to this case as they did not take effect until after this bankruptcy, would deem the claims identified in this case as equity claims. The amendments reflect the trend in case authority in the characterization of equity claims. Section 2 of the *BIA* now defines such claims as follows:

> "equity claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
>
> (b) a return of capital,
>
> (c) a redemption or retraction obligation,
>
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
>
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d).

[18] Given all of the foregoing, I conclude that the claims as set out in paragraphs 3(a), (b), and (c) above should be disallowed.

[19] The claims as set out in paragraphs 3(d) and (e) should be disallowed on the basis that the claims are in relation to investments for preferred shares and limited partnership in Dexior (SVG) Ltd. and Dexior Centrepoint Limited Partnership and should be advanced against those other entities.

[20] In terms of the claims in paragraph 3(f), these should be disallowed as they are so closely connected with the underlying equity claim that they should be treated as such and should be disallowed. See for example: *Blue Range* and *Merit Energy*.

Conclusion

[21] The Trustee's is authorized to disallow the claims that he has identified in this application.

"The Honourable Mr. Justice Masuhara"

TAB 14

CITATION: Nelson Financial Group Ltd., 2010 ONSC 6229
COURT FILE NO.: 10-8630-00CL
DATE: 20101116

ONTARIO

SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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

AND IN THE MATTER OFA PLAN OF COMPROMISE OR ARRANGEMENT OF NELSON FINANCIAL GROUP LTD.

COUNSEL: *Richard B. Jones and Douglas Turner, Q.C.* Representative Counsel for Noteholders/Moving Party
J.H. Grout and S. Aggarwal for the Monitor
Pamela Foy for the Ontario Securities Commission
Frank Lamie for Nelson Financial Group Ltd.
Robert Benjamin Mills and Harold Van Winssen for Clifford Styles, Jackie Styles and Play Investments Ltd., Respondents
Michael Beardsley, Self Represented Respondent
Clifford Holland, Self Represented Respondent
Arnold Bolliger, Self Represented Respondent
John McVey, Self Represented Respondent
Joan Frederick, Self Represented Respondent
Rakesh Sharma, Self Represented Respondent
Larry Debono, Self Represented Respondent
Keith McClear, Self Represented Respondent

REASONS FOR DECISION

PEPALL J.

[1] This motion addresses the legal characterization of claims of holders of preferred shares in the capital stock of the applicant, Nelson Financial Group Ltd. ("Nelson"). The issue before me is to determine whether such claims constitute equity claims for the purposes of sections 6(8) and 22.1 of the *Companies' Creditors Arrangement Act* ("*CCAA*").

Background Facts

[2] Nelson was incorporated pursuant to the *Business Corporations Act* of Ontario in September, 1990. Nelson raised money from investors and then used those funds to extend credit to customers in vendor assisted financing programmes. It raised money in two ways. It issued promissory notes bearing a rate of return of 12% per annum and also issued preference shares typically with an annual dividend of 10%.[1] The funds were then lent out at significantly higher rates of interest.

[3] The Monitor reported that Nelson placed ads in selected publications. The ads outlined the nature of the various investment options. Term sheets for the promissory notes or the preferred shares were then provided to the investors by Nelson together with an outline of the proposed tax treatment for the investment. No funds have been raised from investors since January 29, 2010.

(a) Noteholders

[4] As of the date of the *CCAA* filing on March 23, 2010, Nelson had issued 685 promissory notes in the aggregate principal amount of $36,583,422.89. The notes are held by approximately 321 people.

[1] The Monitor is aware of six preferred shareholders with dividends that ranged from 10.5% to 13.75% per annum.

(b) Preferred Shareholders

[5] Nelson was authorized to issue two classes of common shares and 2,800,000 Series A preferred shares and 2,000,000 Series B preferred shares, each with a stated capital of $25.00. The president and sole director of Nelson, Marc Boutet, is the owner of all of the issued and outstanding common shares. By July 31, 2007, Nelson had issued to investors 176,675 Series A preferred shares for an aggregate consideration of $4,416,925. During the subsequent fiscal year ended July 31, 2008, Nelson issued a further 172,545 Series A preferred shares and 27,080 Series B preferred shares. These shares were issued for an aggregate consideration of $4,672,383 net of share issue costs.

[6] The preferred shares are non-voting and take priority over the common shares. The company's articles of amendment provide that the preferred shareholders are entitled to receive fixed preferential cumulative cash dividends at the rate of 10% per annum. Nelson had the unilateral right to redeem the shares on payment of the purchase price plus accrued dividends. At least one investor negotiated a right of redemption. Two redemption requests were outstanding as of the *CCAA* filing date.

[7] As of the *CCAA* filing date of March 23, 2010, Nelson had issued and outstanding 585,916.6 Series A and Series B preferred shares with an aggregate stated capital of $14,647,914. The preferred shares are held by approximately 82 people. As of the date of filing of these *CCAA* proceedings, there were approximately $53,632 of declared but unpaid dividends outstanding with respect to the preferred shares and $73,652.51 of accumulated dividends.

[8] Investors subscribing for preferred shares entered into subscription agreements described as term sheets. These were executed by the investor and by Nelson. Nelson issued share certificates to the investors and maintained a share register recording the name of each preferred shareholder and the number of shares held by each shareholder.

[9] As reported by the Monitor, notwithstanding that Nelson issued two different series of preferred shares, the principal terms of the term sheets signed by the investors were almost identical and generally provided as follows:

- the issuer was Nelson;
- the par value was fixed at $25.00;
- the purpose was to finance Nelson's business operations;
- the dividend was 10% per annum, payable monthly, commencing one month after the investment was made;
- preferred shareholders were eligible for a dividend tax credit;
- Nelson issued annual T-3 slips on account of dividend income to the preferred shareholders;
- the preferred shares were non-voting (except where voting as a class was required), redeemable at the option of Nelson and ranked ahead of common shares; and
- dividends were cumulative and no dividends were to be paid on common shares if preferred share dividends were in arrears.

[10] In addition, the Series B term sheet provided that the monthly dividend could be reinvested pursuant to a Dividend Reinvestment Plan ("DRIP").

[11] The preferred shareholders were entered on the share register and received share certificates. They were treated as equity in the company's financial statements. Dividends were received by the preferred shareholders and they took the benefit of the advantageous tax treatment.

(c) Insolvency

[12] Mr. Boutet knew that Nelson was insolvent since at least its financial year ended July 31, 2007. Nelson did not provide financial statements to any of the preferred shareholders prior to, or subsequent to, the making of the investment.

(d) Ontario Securities Commission

[13] On May 12, 2010, the Ontario Securities Commission ("OSC") issued a Notice of Hearing and Statement of Allegations alleging that Nelson and its affiliate, Nelson Investment Group Ltd., and various officers and directors of those corporations committed breaches of the *Ontario Securities Act* in the course of selling preferred shares. The allegations include non-compliance with the prospectus requirements, the sale of shares in reliance upon exemptions that were inapplicable, the sale of shares to persons who were not accredited investors, and fraudulent and negligent misrepresentations made in the course of the sale of shares. The OSC hearing has been scheduled for the end of February, 2011.

(e) Legal Opinion

[14] Based on the Monitor's review, the preferred shareholders were documented as equity on Nelson's books and records and financial statements. Pursuant to court order, the Monitor

retained Stikeman Elliott LLP as independent counsel to provide an opinion on the characterization of the claims and potential claims of the preferred shareholders. The opinion concluded that the claims were equity claims. The Monitor posted the opinion on its website and also advised the preferred shareholders of the opinion and conclusions by letter. The opinion was not to constitute evidence, issue estoppel or res judicata with respect to any matters of fact or law referred to therein. The opinion, at least in part, informed Nelson's position which was supported by the Monitor, that independent counsel for the preferred shareholders was unwarranted in the circumstances.

(f) Development of Plan

[15] The Monitor reported in its Eighth Report that a plan is in the process of being developed and that preferred shareholders would have their existing preference shares cancelled and would then be able to claim a tax loss on their investment or be given a new form of preference shares with rights to be determined.

Motion

[16] The holders of promissory notes are represented by Representative Counsel appointed pursuant to my order of June 15, 2010. Representative Counsel wishes to have some clarity as to the characterization of the preferred shareholders' claims. Accordingly, Representative Counsel has brought a motion for an order that all claims and potential claims of the preferred shareholders against Nelson be classified as equity claims within the meaning of the *CCAA*. In addition, Representative Counsel requests that the unsecured creditors, which include the noteholders, be entitled to be paid in full before any claim of a preferred shareholder and that the

preferred shareholders form a separate class that is not entitled to vote at any meeting of creditors. Nelson and the Monitor support the position of Representative Counsel. The OSC is unopposed.

[17] On the return of the motion, some preferred shareholders were represented by counsel from Templeman Menninga LLP and some were self-represented. It was agreed that the letters and affidavits of preferred shareholders that were filed with the court would constitute their evidence. Oral submissions were made by legal counsel and by approximately eight individuals. They had many complaints. Their allegations against Nelson and Mr. Boutet range from theft, fraud, misrepresentation including promises that their funds would be secured, operation of a Ponzi scheme, breach of trust, dividend payments to some that exceeded the rate set forth in Nelson's articles, conversion of notes into preferred shares at a time when Nelson was insolvent, non-disclosure, absence of a prospectus or offering memorandum disclosure, oppression, violation of section 23(3) of the *OBCA* and of the *Securities Act* such that the issuance of the preferred shares was a nullity, and breach of fiduciary duties.

[18] The stories described by the investors are most unfortunate. Many are seniors and pensioners who have invested their savings with Nelson. Some investors had notes that were rolled over and replaced with preference shares. Mr. McVey alleges that he made an original promissory note investment which was then converted arbitrarily and without his knowledge into preference shares. He alleges that the documents effecting the conversion did not contain his authentic signature.

[19] Mr. Styles states that he and his company invested approximately $4.5 million in Nelson. He states that Mr. Boutet persuaded him to convert his promissory notes into preference shares by promising a 13.75% dividend rate, assuring him that the obligation of Nelson to repay would be treated the same or better than the promissory notes, and that they would have the same or a priority position to the promissory notes. He then received dividends at the 13.75% rate contrary to the 10% rate found in the company's articles. In addition, at the time of the conversion, Nelson was insolvent.

[20] In brief, Mr. Styles submits that:

(a) the investment transactions were void because there was no prospectus contrary to the provisions of the *Securities Act* and the Styles were not accredited investors; the preferred shares were issued contrary to section 23(3) of the *OBCA* in that Nelson was insolvent at the relevant time and as such, the issuance was a nullity; and the conduct of the company and its principal was oppressive contrary to section 248 of the *OBCA*; and that

(b) the Styles' claim is in respect of an undisputed agreement relating to the conversion of their promissory notes into preferred shares which agreement is enforceable separate and apart from any claim relating to the preferred shares.

The Issue

[21] Are any of the claims advanced by the preferred shareholders equity claims within section 2 of the *CCAA* such that they are to be placed in a separate class and are subordinated to the full recovery of all other creditors?

The Law

[22] The relevant provisions of the *CCAA* are as follows.

Section 2 of the *CCAA* states:

> In this Act,
>
> "Claim" means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the *Bankruptcy and Insolvency Act*;
>
> "Equity Claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
>
> (b) a return of capital,
>
> (c) a redemption or retraction obligation,
>
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
>
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (*a*) to (*d*);"
>
> "Equity Interest" means
>
> (a) in the case of a corporation other than an income trust, a share in the corporation — or a warrant or option or another right to acquire a share in the corporation — other than one that is derived from a convertible debt, and
>
> (b) in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt;

Section 6(8) states:

> No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

Section 22.1 states:

> Despite subsection 22(1) creditors having equity claims are to be in the same class of creditors in relation to those claims unless the court orders otherwise and may not, as members of that class, vote at any meeting unless the court orders otherwise.

[23] Section 2 of the *Bankruptcy and Insolvency Act* ("*BIA*") which is referenced in section 2 of the *CCAA* provides that a claim provable includes any claim or liability provable in proceedings under the Act by a creditor. Creditor is then defined as a person having a claim provable as a claim under the Act.

[24] Section 121(1) of the *BIA* describes claims provable. It states:

> All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

[25] Historically, the claims and rights of shareholders were not treated as provable claims and ranked after creditors of an insolvent corporation in a liquidation. As noted by Laskin J.A. in *Re Central Capital Corporation*[2], on the insolvency of a company, the claims of creditors have always ranked ahead of the claims of shareholders for the return of their capital. This

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[2] (1996), 38 C.B.R. (3d) 1 (Ont. C.A.).

principle is premised on the notion that shareholders are understood to be higher risk participants who have chosen to tie their investment to the fortunes of the corporation. In contrast, creditors choose a lower level of exposure, the assumption being that they will rank ahead of shareholders in an insolvency. Put differently, amongst other things, equity investors bear the risk relating to the integrity and character of management.

[26] This treatment also has been held to encompass fraudulent misrepresentation claims advanced by a shareholder seeking to recover his investment: *Re Blue Range Resource Corp.*[3] In that case, Romaine J. held that the alleged loss derived from and was inextricably intertwined with the shareholder interest. Similarly, in the United States, the Second Circuit Court of Appeal in *Re Stirling Homex Corp.*[4] concluded that shareholders, including those who had allegedly been defrauded, were subordinate to the general creditors when the company was insolvent. The Court stated that "the real party against which [the shareholders] are seeking relief is the body of general creditors of their corporation. Whatever relief may be granted to them in this case will reduce the percentage which the general creditors will ultimately realize upon their claims." *National Bank of Canada v. Merit Energy Ltd.*[5] and *Earthfirst Canada Inc.*[6] both treated claims relating to agreements that were collateral to equity claims as equity claims. These cases dealt

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[3] 2000, 15 C.B.R. (4th) 169.

[4] (1978) 579 F. 2d 206 (2nd Cir. Ct. of App.).

[5] (2001), 2001 CarswellAlta. 913, aff'd 2002 CarswellAlta 23 (Alta C.A.).

[6] (2009) 2009 CarswellAlta 1069.

with separate indemnification agreements and the issuance of flow through shares. The separate agreements and the ensuing claims were treated as part of one integrated transaction in respect of an equity interest. The case law has also recognized the complications and delay that would ensue if *CCAA* proceedings were mired in shareholder claims.

[27] The amendments to the *CCAA* came into force on September 18, 2009. It is clear that the amendments incorporated the historical treatment of equity claims. The language of section 2 is clear and broad. Equity claim means a claim in respect of an equity interest and includes, amongst other things, a claim for rescission of a purchase or sale of an equity interest. Pursuant to sections 6(8) and 22.1, equity claims are rendered subordinate to those of creditors.

[28] The Nelson filing took place after the amendments and therefore the new provisions apply to this case. Therefore, if the claims of the preferred shareholders are properly characterized as equity claims, the relief requested by Representative Counsel in his notice of motion should be granted.

[29] Guidance on the appropriate approach to the issue of characterization was provided by the Ontario Court of Appeal in *Re Central Capital Corporation*[7]. Central Capital was insolvent and sought protection pursuant to the provisions of the *CCAA*. The appellants held preferred shares of Central Capital. The shares each contained a right of retraction, that is, a right to require Central Capital to redeem the shares on a fixed date and for a fixed price. One

[7] Supra, note 2.

shareholder exercised his right of retraction and the other shareholder did not but both filed proofs of claim in the *CCAA* proceedings. In considering whether the two shareholders had provable debt claims, Laskin J.A. considered the substance of the relationship between the company and the shareholders. If the governing instrument contained features of both debt and equity, that is, it was hybrid in character, the court must determine the substance of the relationship between the company and the holder of the certificate. The Court examined the parties' intentions.

[30] In *Central Capital*, Laskin J.A. looked to the share purchase agreements, the conditions attaching to the shares, the articles of incorporation and the treatment given to the shares in the company's financial statements to ascertain the parties' intentions and determined that the claims were equity and not debt claims.

[31] In this case, there are characteristics that are suggestive of a debt claim and of an equity claim. That said, in my view, the preferred shareholders are, as their description implies, shareholders of Nelson and not creditors. In this regard, I note the following.

(a) Investors were given the option of investing in promissory notes or preference shares and opted to invest in shares. Had they taken promissory notes, they obviously would have been creditors. The preference shares carried many attractions including income tax advantages.

(b) The investors had the right to receive dividends, a well recognized right of a shareholder.

(c) The preference share conditions provided that on a liquidation, dissolution or winding up, the preferred shareholders ranked ahead of common shareholders. As in *Central Capital*, it is implicit that they therefore would rank behind creditors.

(d) Although I acknowledge that the preferred shareholders did not receive copies of the financial statements, nonetheless, the shares were treated as equity in Nelson's financial statements and in its books and records.

[32] The substance of the arrangement between the preferred shareholders and Nelson was a relationship based on equity and not debt. Having said that, as I observed in *I. Waxman & Sons.*[8], there is support in the case law for the proposition that equity may become debt. For instance, in that case, I held that a judgment obtained at the suit of a shareholder constituted debt. An analysis of the nature of the claims is therefore required. If the claims fall within the parameters of section 2 of the *CCAA*, clearly they are to be treated as equity claims and not as debt claims.

[33] In this case, in essence the claims of the preferred shareholders are for one or a combination of the following:

(a) declared but unpaid dividends;

(b) unperformed requests for redemption;

(c) compensatory damages for the loss resulting in the purchased preferred shares now being worthless and claimed to have been caused by the negligent or fraudulent

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[8] (2008), 2008 CarswellOnt 1245.

misrepresentation of Nelson or of persons for whom Nelson is legally responsible; and

(d) payment of the amounts due upon the rescission or annulment of the purchase or subscription for preferred shares.

[34] In my view, all of these claims fall within the ambit of section 2, are governed by sections 6(8) and 22.1 of the *CCAA*, and therefore do not constitute a claim provable for the purposes of the statute. The language of section 2 is clear and unambiguous and equity claims include "a claim that is in respect of an equity interest" and a claim for a dividend or similar payment and a claim for rescission. This encompasses the claims of all of the preferred shareholders including the Styles whose claim largely amounts to a request for rescission or is in respect of an equity interest. The case of *National Bank of Canada v. Merit Energy Ltd.*[9] is applicable in regard to the latter. In substance, the Styles' claim is for an equity obligation. At a minimum, it is a claim in respect of an equity interest as described in section 2 of the CCAA. Parliament's intention is clear and the types of claims advanced in this case by the preferred shareholders are captured by the language of the amended statute. While some, and most notably Professor Janis Sarra[10], advocated a statutory amendment that provided for some judicial flexibility in cases involving damages arising from egregious conduct on the part of a debtor corporation and its officers, Parliament opted not to include such a provision. Sections 6(8) and

[9] Supra, note 5.

[10] "From Subordination to Parity: An International Comparison of Equity Securities Law Claims in Insolvency Proceedings" (2007) 16 Int. Insolv. Re., 181.

22.1 allow for little if any flexibility. That said, they do provide for greater certainty in the appropriate treatment to be accorded equity claims.

[35] There are two possible exceptions. Mr. McVey claims that his promissory note should never have been converted into preference shares, the conversion was unauthorized and that the signatures on the term sheets are not his own. If Mr. McVey's evidence is accepted, his claim would be qua creditor and not preferred shareholder. Secondly, it is possible that monthly dividends that may have been lent to Nelson by Larry Debono constitute debt claims. The factual record on these two possible exceptions is incomplete. The Monitor is to investigate both scenarios, consider a resolution of same, and report back to the court on notice to any affected parties.

[36] Additionally, the claims procedure will have to be amended. The Monitor should consider an appropriate approach and make a recommendation to the court to accommodate the needs of the stakeholders. The relief requested in the notice of motion is therefore granted subject to the two aforesaid possible exceptions.

Pepall J.

Released: November 16, 2010

CITATION: Nelson Financial Group Ltd., 2010 ONSC 6229
COURT FILE NO.: 10-8630-00CL
DATE: 20101116

ONTARIO

SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

BETWEEN:

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

AND IN THE MATTER OFA PLAN OF COMPROMISE OR ARRANGEMENT OF NELSON FINANCIAL GROUP LTD.

REASONS FOR JUDGMENT

Pepall J.

Released: November 16, 2010

TAB 15

CITATION: Sino-Forest Corporation (Re), 2012 ONSC 4377
COURT FILE NO.: CV-12-9667-00CL
DATE: 20120727

SUPERIOR COURT OF JUSTICE – ONTARIO

(COMMERCIAL LIST)

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

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

BEFORE: **MORAWETZ J.**

COUNSEL: **Robert W. Staley and Jonathan Bell, for the Applicant**

Jennifer Stam, for the Monitor

Kenneth Dekker, for BDO Limited

Peter Griffin and Peter Osborne, for Ernst & Young LLP

Benjamin Zarnett, Robert Chadwick and Brendan O'Neill, for the Ad Hoc Committee of Noteholders

James Grout, for the Ontario Securities Commission

Emily Cole and Joseph Marin, for Allen Chan

Simon Bieber, for David Horsley

David Bish, John Fabello and Adam Slavens, for the Underwriters Named in the Class Action

Max Starnino and Kirk Baert, for the Ontario Plaintiffs

Larry Lowenstein, for the Board of Directors

HEARD: **June 26, 2012**

ENDORSEMENT

Overview

[1] Sino-Forest Corporation ("SFC" or the "Applicant") seeks an order directing that claims against SFC, which result from the ownership, purchase or sale of an equity interest in SFC, are "equity claims" as defined in section 2 of the *Companies' Creditors Arrangement Act* ("CCAA") including, without limitation: (i) the claims by or on behalf of current or former shareholders asserted in the proceedings listed in Schedule "A" (collectively, the "Shareholder Claims"); and (ii) any indemnification claims against SFC related to or arising from the Shareholder Claims, including, without limitation, those by or on behalf of any of the other defendants to the proceedings listed in Schedule "A" (the "Related Indemnity Claims").

[2] SFC takes the position that the Shareholder Claims are "equity claims" as defined in the CCAA as they are claims in respect of a monetary loss resulting from the ownership, purchase or sale of an equity interest in SFC and, therefore, come within the definition. SFC also takes the position that the Related Indemnity Claims are "equity claims" as defined in the CCAA as they are claims for contribution or indemnity in respect of a claim that is an equity claim and, therefore, also come within the definition.

[3] On March 30, 2012, the court granted the Initial Order providing for the CCAA stay against SFC and certain of its subsidiaries. FTI Consulting Canada Inc. was appointed as Monitor.

[4] On the same day, the Sales Process Order was granted, approving Sales Process procedures and authorizing and directing SFC, the Monitor and Houlihan Lokey to carry out the Sales Process.

[5] On May 14, 2012, the court issued a Claims Procedure Order, which established June 20, 2012 as the Claims Bar Date.

[6] The stay of proceedings has since been extended to September 28, 2012.

[7] Since the outset of the proceedings, SFC has taken the position that it is important for these proceedings to be completed as soon as possible in order to, among other things, (i) enable the business operated in the Peoples Republic of China ("PRC") to be separated from SFC and put under new ownership; (ii) enable the restructured business to participate in the Q4 sales season in the PRC market; and (iii) maintain the confidence of stakeholders in the PRC (including local and national governmental bodies, PRC lenders and other stakeholders) that the business in the PRC can be successfully separated from SFC and operate in the ordinary course in the near future.

[8] SFC has negotiated a Support Agreement with the Ad Hoc Committee of Noteholders and intends to file a plan of compromise or arrangement (the "Plan") under the CCAA by no later than August 27, 2012, based on the deadline set out in the Support Agreement and what

they submit is the commercial reality that SFC must complete its restructuring as soon as possible.

[9] Noteholders holding in excess of $1.296 billion, or approximately 72% of the approximately $1.8 billion of SFC's noteholders' debt, have executed written support agreements to support the SFC CCAA Plan as of March 30, 2012.

Shareholder Claims Asserted Against SFC

(i) Ontario

[10] By Fresh as Amended Statement of Claim dated April 26, 2012 (the "Ontario Statement of Claim"), the Trustees of the Labourers' Pension Fund of Central and Eastern Canada and other plaintiffs asserted various claims in a class proceeding (the "Ontario Class Proceedings") against SFC, certain of its current and former officers and directors, Ernst & Young LLP ("E&Y"), BDO Limited ("BDO"), Poyry (Beijing) Consulting Company Limited ("Poyry") and SFC's underwriters (collectively, the "Underwriters").

[11] Section 1(m) of the Ontario Statement of Claim defines "class" and "class members" as:

> All persons and entities, wherever they may reside who acquired Sino's Securities during the Class Period by distribution in Canada or on the Toronto Stock Exchange or other secondary market in Canada, which securities include those acquired over the counter, and all persons and entities who acquired Sino's Securities during the Class Period who are resident of Canada or were resident of Canada at the time of acquisition and who acquired Sino's Securities outside of Canada, except the Excluded Persons.

[12] The term "Securities" is defined as "Sino's common shares, notes and other securities, as defined in the OSA". The term "Class Period" is defined as the period from and including March 19, 2007 up to and including June 2, 2011.

[13] The Ontario Class Proceedings seek damages in the amount of approximately $9.2 billion against SFC and the other defendants.

[14] The thrust of the complaint in the Ontario Class Proceedings is that the class members are alleged to have purchased securities at "inflated prices during the Class Period" and that absent the alleged misconduct, sales of such securities "would have occurred at prices that reflected the true value" of the securities. It is further alleged that "the price of Sino's Securities was directly affected during the Class Period by the issuance of the Impugned Documents".

(ii) Quebec

[15] By action filed in Quebec on June 9, 2011, Guining Liu commenced an action (the "Quebec Class Proceedings") against SFC, certain of its current and former officers and directors, E&Y and Poyry. The Quebec Class Proceedings do not name BDO or the

Underwriters as defendants. The Quebec Class Proceedings also do not specify the quantum of damages sought, but rather reference "damages in an amount equal to the losses that it and the other members of the group suffered as a result of purchasing or acquiring securities of Sino at inflated prices during the Class Period".

[16] The complaints in the Quebec Class Proceedings centre on the effect of alleged misrepresentations on the share price. The duty allegedly owed to the class members is said to be based in "law and other provisions of the *Securities Act*", to ensure the prompt dissemination of truthful, complete and accurate statements regarding SFC's business and affairs and to correct any previously-issued materially inaccurate statements.

(iii) Saskatchewan

[17] By Statement of Claim dated December 1, 2011 (the "Saskatchewan Statement of Claim"), Mr. Allan Haigh commenced an action (the "Saskatchewan Class Proceedings") against SFC, Allen Chan and David Horsley.

[18] The Saskatchewan Statement of Claim does not specify the quantum of damages sought, but instead states in more general terms that the plaintiff seeks "aggravated and compensatory damages against the defendants in an amount to be determined at trial".

[19] The Saskatchewan Class Proceedings focus on the effect of the alleged wrongful acts upon the trading price of SFC's securities:

> The price of Sino's securities was directly affected during the Class Period by the issuance of the Impugned Documents. The defendants were aware at all material times that the effect of Sino's disclosure documents upon the price of its Sino's [sic] securities.

(iv) New York

[20] By Verified Class Action Complaint dated January 27, 2012, (the "New York Complaint"), Mr. David Leapard and IMF Finance SA commenced a class proceeding against SFC, Mr. Allen Chan, Mr. David Horsley, Mr. Kai Kit Poon, a subset of the Underwriters, E&Y, and Ernst & Young Global Limited (the "New York Class Proceedings").

[21] SFC contends that the New York Class Proceedings focus on the effect of the alleged wrongful acts upon the trading price of SFC's securities.

[22] The plaintiffs in the various class actions have named parties other than SFC as defendants, notably, the Underwriters and the auditors, E&Y, and BDO, as summarized in the table below. The positions of those parties are detailed later in these reasons.

	Ontario	Quebec	Saskatchewan	New York

E&Y LLP	X	X	-	X
E&Y Global	-	-	-	X
BDO	X	-	-	-
Poyry	X	X	-	-
Underwriters	11	-	-	2

Legal Framework

[23] Even before the 2009 amendments to the CCAA dealing with equity claims, courts recognized that there is a fundamental difference between shareholder equity claims as they relate to an insolvent entity versus creditor claims. Essentially, shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditor claims are not being paid in full. Simply put, shareholders have no economic interest in an insolvent enterprise: *Blue Range Resource Corp. (Re)*, (2004) 4 W.W.R. 738 (Alta. Q.B.) [*Blue Range Resources*]; *Stelco Inc. (Re)*, (2006) CanLII 1773 (Ont. S.C.J.) [*Stelco*]; *Royal Bank of Canada v. Central Capital Corp*. (1996), 27 O.R. (3d) 494 (C.A.).

[24] The basis for the differentiation flows from the fundamentally different nature of debt and equity investments. Shareholders have unlimited upside potential when purchasing shares. Creditors have no corresponding upside potential: *Nelson Financial Group Limited (Re)*, 2010 ONSC 6229 [*Nelson Financial*].

[25] As a result, courts subordinated equity claims and denied such claims a vote in plans of arrangement: *Blue Range Resource*, *supra*; *Stelco*, *supra*; *EarthFirst Canada Inc. (Re)* (2009), 56 C.B.R. (5th) 102 (Alta. Q.B.) [*EarthFirst Canada*]; and *Nelson Financial*, *supra*.

[26] In 2009, significant amendments were made to the CCAA. Specific amendments were made with the intention of clarifying that equity claims are subordinated to other claims.

[27] The 2009 amendments define an "equity claim" and an "equity interest". Section 2 of the CCAA includes the following definitions:

> "Equity Claim" means a claim that is in respect of an equity interest, including a claim for, among others, (…)
>
> > (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or

> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);
>
> "Equity Interest" means
>
> (a) in the case of a company other than an income trust, a share in the company – or a warrant or option or another right to acquire a share in the company – other than one that is derived from a convertible debt,

[28] Section 6(8) of the CCAA prohibits a distribution to equity claimants prior to payment in full of all non-equity claims.

[29] Section 22(1) of the CCAA provides that equity claimants are prohibited from voting on a plan unless the court orders otherwise.

Position of Ernst & Young

[30] E&Y opposes the relief sought, at least as against E&Y, since the E&Y proof of claim evidence demonstrates in its view that E&Y's claim:

(a) is not an equity claim;

(b) does not derive from or depend upon an equity claim (in whole or in part);

(c) represents discreet and independent causes of action as against SFC and its directors and officers arising from E&Y's direct contractual relationship with such parties (or certain of such parties) and/or the tortious conduct of SFC and/or its directors and officers for which they are in law responsible to E&Y; and

(d) can succeed independently of whether or not the claims of the plaintiffs in the class actions succeed.

[31] In its factum, counsel to E&Y acknowledges that during the periods relevant to the Class Action Proceedings, E&Y was retained as SFC's auditor and acted as such from 2007 until it resigned on April 5, 2012.

[32] On June 2, 2011, Muddy Waters LLC ("Muddy Waters") issued a report which purported to reveal fraud at SFC. In the wake of that report, SFC's share price plummeted and Muddy Waters profited from its short position.

[33] E&Y was served with a multitude of class action claims in numerous jurisdictions.

[34] The plaintiffs in the Ontario Class Proceedings claim damages in the aggregate, as against all defendants, of $9.2 billion on behalf of resident and non-resident shareholders and noteholders. The causes of action alleged are both statutory, under the *Securities Act (Ontario)* and at common law, in negligence and negligent misrepresentation.

[35] In its factum, counsel to E&Y acknowledges that the central claim in the class actions is that SFC made a series of misrepresentations in respect of its timber assets. The claims against E&Y and the other third party defendants are that they failed to detect these misrepresentations and note in particular that E&Y's audit did not comply with Canadian generally accepted accounting standards. Similar claims are advanced in Quebec and the U.S.

[36] Counsel to E&Y notes that on May 14, 2012 the court granted a Claims Procedure Order which, among other things, requires proofs of claim to be filed no later than June 20, 2012. E&Y takes issue with the fact that this motion was then brought notwithstanding that proofs of claim and D&O proofs of claim had not yet been filed.

[37] E&Y has filed with the Monitor, in accordance with the Claims Procedure Order, a proof of claim against SFC and a proof of claim against the directors and officers of SFC.

[38] E&Y takes the position that it has contractual claims of indemnification against SFC and its subsidiaries and has statutory and common law claims of contribution and/or indemnity against SFC and its subsidiaries for all relevant years. E&Y contends that it has stand-alone claims for breach of contract and negligent and/or fraudulent misrepresentation against the company and its directors and officers.

[39] Counsel submits that E&Y's claims against Sino-Forest and the SFC subsidiaries are:

(a) creditor claims;

(b) derived from E&Y retainers by and/or on behalf of Sino-Forest and the SFC subsidiaries and E&Y's relationship with such parties, all of which are wholly independent and conceptually different from the claims advanced by the class action plaintiffs;

(c) claims that include the cost of defending and responding to various proceedings, both pre- and post-filing; and

(d) not equity claims in the sense contemplated by the CCAA. E&Y's submission is that equity holders of Sino-Forest have not advanced, and could not advance, any claims against SFC's subsidiaries.

[40] Counsel further contends that E&Y's claim is distinct from any and all potential and actual claims by the plaintiffs in the class actions against Sino-Forest and that E&Y's claim for contribution and/or indemnity is not based on the claims against Sino-Forest advanced in the class actions but rather only in part on those claims, as any success of the plaintiffs in the class actions against E&Y would not necessarily lead to success against Sino-Forest, and vice versa. Counsel contends that E&Y has a distinct claim against Sino-Forest independent of that of the plaintiffs in the class actions. The success of E&Y's claims against Sino-Forest and the SFC subsidiaries, and the success of the claims advanced by the class action plaintiffs, are not co-dependent. Consequently, counsel contends that E&Y's claim is that of an unsecured creditor.

[41] From a policy standpoint, counsel to E&Y contends that the nature of the relationship between a shareholder, who may be in a position to assert an equity claim (in addition to other claims) is fundamentally different from the relationship existing between a corporation and its auditors.

Position of BDO Limited

[42] BDO was auditor of Sino-Forest Corporation between 2005 and 2007, when it was replaced by E&Y.

[43] BDO has a filed a proof of claim against Sino-Forest pursuant to the Claims Procedure Order.

[44] BDO's claim against Sino-Forest is primarily for breach of contract.

[45] BDO takes the position that its indemnity claims, similar to those advanced by E&Y and the Underwriters, are not equity claims within the meaning of s. 2 of the CCAA.

[46] BDO adopts the submissions of E&Y which, for the purposes of this endorsement, are not repeated.

Position of the Underwriters

[47] The Underwriters take the position that the court should not decide the equity claims motion at this time because it is premature or, alternatively, if the court decides the equity claims motion, the equity claims order should not be granted because the Related Indemnity Claims are not "equity claims" as defined in s. 2 of the CCAA.

[48] The Underwriters are among the defendants named in some of the class actions. In connection with the offerings, certain Underwriters entered into agreements with Sino-Forest and certain of its subsidiaries providing that Sino-Forest and, with respect to certain offerings, the Sino-Forest subsidiary companies, agree to indemnify and hold harmless the Underwriters in connection with an array of matters that could arise from the offerings.

[49] The Underwriters raise the following issues:

(i) Should this court decide the equity claims motion at this time?

(ii) If this court decides the equity claims motion at this time, should the equity claims order be granted?

[50] On the first issue, counsel to the Underwriters takes the position that the issue is not yet ripe for determination.

[51] Counsel submits that, by seeking the equity claims order at this time, Sino-Forest is attempting to pre-empt the Claims Procedure Order, which already provides a process for the

determination of claims. Until such time as the claims procedure in respect of the Related Indemnity Claims is completed, and those claims are determined pursuant to that process, counsel contends the subject of the equity claims motion raises a merely hypothetical question as the court is being asked to determine the proper interpretation of s. 2 of the CCAA before it has the benefit of an actual claim in dispute before it.

[52] Counsel further contends that by asking the court to render judgment on the proper interpretation of s. 2 of the CCAA in the hypothetical, Sino-Forest has put the court in a position where its judgment will not be made in the context of particular facts or with a full and complete evidentiary record.

[53] Even if the court determines that it can decide this motion at this time, the Underwriters submit that the relief requested should not be granted.

Position of the Applicant

[54] The Applicant submits that the amendments to the CCAA relating to equity claims closely parallel existing U.S. law on the subject and that Canadian courts have looked to U.S. courts for guidance on the issue of equity claims as the subordination of equity claims has long been codified there: see e.g. *Blue Range Resources, supra*, and *Nelson Financial, supra*.

[55] The Applicant takes the position that based on the plain language of the CCAA, the Shareholder Claims are "equity claims" as defined in s. 2 as they are claims in respect of a "monetary loss resulting from the ownership, purchase or sale of an equity interest".

[56] The Applicant also submits the following:

(a) the Ontario, Quebec, Saskatchewan and New York Class Actions (collectively, the "Class Actions") all advance claims on behalf of shareholders.

(b) the Class Actions also allege wrongful conduct that affected the trading price of the shares, in that the alleged misrepresentation "artificially inflated" the share price; and

(c) the Class Actions seek damages relating to the trading price of SFC shares and, as such, allege a "monetary loss" that resulted from the ownership, purchase or sale of shares, as defined in s. 2 of the CCAA.

[57] Counsel further submits that, as the Shareholder Claims are "equity claims", they are expressly subordinated to creditor claims and are prohibited from voting on the plan of arrangement.

[58] Counsel to the Applicant also submits that the definition of "equity claims" in s. 2 of the CCAA expressly includes indemnity claims that relate to other equity claims. As such, the Related Indemnity Claims are equity claims within the meaning of s. 2.

[59] Counsel further submits that there is no distinction in the CCAA between the source of any claim for contribution or indemnity; whether by statute, common law, contractual or otherwise. Further, and to the contrary, counsel submits that the legal characterization of a contribution or indemnity claim depends solely on the characterization of the primary claim upon which contribution or indemnity is sought.

[60] Counsel points out that in *Return on Innovation Capital v. Gandi Innovations Limited*, 2011 ONSC 5018, leave to appeal denied, 2012 ONCA 10 [*Return on Innovation*] this court characterized the contractual indemnification claims of directors and officers in respect of an equity claim as "equity claims".

[61] Counsel also submits that guidance on the treatment of underwriter and auditor indemnification claims can be obtained from the U.S. experience. In the U.S., courts have held that the indemnification claims of underwriters for liability or defence costs constitute equity claims that are subordinated to the claims of general creditors. Counsel submits that insofar as the primary source of liability is characterized as an equity claim, so too is any claim for contribution and indemnity based on that equity claim.

[62] In this case, counsel contends, the Related Indemnity Claims are clearly claims for "contribution and indemnity" based on the Shareholder Claims.

Position of the Ad Hoc Noteholders

[63] Counsel to the Ad Hoc Noteholders submits that the Shareholder Claims are "equity claims" as they are claims in respect of an equity interest and are claims for "a monetary loss resulting from the ownership, purchase or sale of an equity interest" per subsection (d) of the definition of "equity claims" in the CCAA.

[64] Counsel further submits that the Related Indemnity Claims are also "equity claims" as they fall within the "clear and unambiguous" language used in the definition of "equity claim" in the CCAA. Subsection (e) of the definition refers expressly and without qualification to claims for "contribution or indemnity" in respect of claims such as the Shareholder Claims.

[65] Counsel further submits that had the legislature intended to qualify the reference to "contribution or indemnity" in order to exempt the claims of certain parties, it could have done so, but it did not.

[66] Counsel also submits that, if the plain language of subsection (e) is not upheld, shareholders of SFC could potentially create claims to receive indirectly what they could not receive directly (*i.e.*, payment in respect of equity claims through the Related Indemnity Claims) – a result that could not have been intended by the legislature as it would be inconsistent with the purposes of the CCAA.

[67] Counsel to the Ad Hoc Noteholders also submits that, before the CCAA amendments in 2009 (the "CCAA Amendments"), courts subordinated claims on the basis of:

(a) the general expectations of creditors and shareholders with respect to priority and assumption of risks; and

(b) the equitable principles and considerations set out in certain U.S. cases: see e.g. *Blue Range Resources, supra*.

[68] Counsel further submits that, before the CCAA Amendments took effect, courts had expanded the types of claims characterized as equity claims; first to claims for damages of defrauded shareholders and then to contractual indemnity claims of shareholders: see *Blue Range Resources, supra* and *EarthFirst Canada, supra*.

[69] Counsel for the Ad Hoc Noteholders also submits that indemnity claims of underwriters have been treated as equity claims in the United States, pursuant to section 510(b) of the U.S. Bankruptcy Code. This submission is detailed at paragraphs 20-25 of their factum which reads as follows:

> 20. The desire to more closely align the Canadian approach to equity claims with the U.S. approach was among the considerations that gave rise to the codification of the treatment of equity claims. Canadian courts have also looked to the U.S. law for guidance on the issue of equity claims where codification of the subordination of equity claims has been long-standing.
>
> Janis Sarra at p. 209, Ad Hoc Committee's Book of Authorities, Tab 10.
>
> Report of the Standing Senate Committee on Banking, Trade and Commerce, "Debtors and Creditors Sharing the Burden: A Review of the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement act*" (2003) at 158, [...]
>
> *Blue Range* [*Resources*] at paras. 41-57 [...]
>
> 21. Pursuant to § 510(b) of the *U.S. Bankruptcy Code*, all creditors must be paid in full before shareholders are entitled to receive any distribution. § 510(b) of the *U.S. Bankruptcy Code* and the relevant portion of § 502, which is referenced in § 510(b), provide as follows:
>
> § 510. Subordination
>
> (b) For the purpose of distribution under this title, a claim arising from rescission of a purchase or sale of a security of the debtor or of an affiliate of the debtor, for damages arising from the purchase or sale of such a security, or for reimbursement or contribution allowed under 502 on account of such a claim, shall be subordinated to all claims or interests that

> are senior to or equal the claim or interest represented by such security, except that if such security is common stock, such claim has the same priority as common stock.
>
> § 502. Allowance of claims or interests
>
> (e) (1) Notwithstanding subsections (a), (b) and (c) of this section and paragraph (2) of this subsection, the court shall disallow any claim for reimbursement or contribution of an entity that is liable with the debtor on or has secured the claim of a creditor, to the extent that
>
> ...
>
> > (B) such claim for reimbursement or contribution is contingent as of the time of allowance or disallowance of such claim for reimbursement or contribution; or
>
> ...
>
> (2) A claim for reimbursement or contribution of such an entity that becomes fixed after the commencement of the case shall be determined, and shall be allowed under subsection (a), (b), or (c) of this section, or disallowed under subsection (d) of this section, the same as if such claim had become fixed before the date of the filing of the petition.

22. U.S. appellate courts have interpreted the statutory language in § 510(b) broadly to subordinate the claims of shareholders that have a nexus or causal relationship to the purchase or sale of securities, including damages arising from alleged illegality in the sale or purchase of securities or from corporate misconduct whether predicated on pre or post-issuance conduct.

> *Re Telegroup Inc.* (2002), 281 F. 3d 133 (3rd Cir. U.S. Court of Appeals) [...]
>
> *American Broadcasting Systems Inc. v. Nugent*, U.S. Court of Appeals for the Ninth Circuit, Case Number 98-17133 (24 January 2001) [...]

23. Further, U.S. courts have held that indemnification claims of underwriters against the corporation for liability or defence costs when shareholders or former shareholders have sued underwriters constitute equity claims in the insolvency of the corporation that are subordinated to the claims of general creditors based on: (a) the plain language of § 510(b), which references claims for "reimbursement or contribution" and (b) risk allocation as between general creditors and those parties that play a role in the purchase and sale of securities that give rise to the shareholder claims (i.e., directors, officers and underwriters).

> *In re Mid-American Waste Sys.*, 228 B.R. 816, 1999 Bankr. LEXIS 27 (Bankr. D. Del. 1999) [*Mid-American*] [...]
>
> *In re Jacom Computer Servs.*, 280 B.R. 570, 2002 Bankr. LEXIS 758 (Bankr. S.D.N.Y. 2002) [...]

24. In *Mid-American*, the Court stated the following with respect to the "plain language" of § 510(b), its origins and the inclusion of "reimbursement or contribution" claims in that section:

> *... I find that the plain language of § 510(b), its legislative history, and applicable case law clearly show that § 510(b) intends to subordinate the indemnification claims of officers, directors, and underwriters for both liability and expenses incurred in connection with the pursuit of claims for rescission or damages by purchasers or sellers of the debtor's securities*. The meaning of amended § 510(b), specifically the language "for reimbursement or contribution . . . on account of [a claim arising from rescission or damages arising from the purchase or sale of a security]," can be discerned by a plain reading of its language.
>
> ... it is readily apparent that the rationale for section 510(b) is not limited to preventing shareholder claimants from improving their position vis-a-vis general creditors; *Congress also made the decision to subordinate based on risk allocation. Consequently, when Congress amended § 510(b) to add reimbursement and contribution claims, it was not radically departing from an equityholder claimant treatment provision, as NatWest suggests; it simply added to the subordination treatment new classes of persons and entities involved with the securities transactions giving rise to the rescission and damage claims*. The 1984 amendment to § 510(b) is a logical extension of one of the rationales for the original section — *because Congress intended the holders of securities law claims to be subordinated, why not also subordinate claims of other parties (e.g., officers and directors and underwriters) who play a role in the purchase and sale transactions which give rise to the securities law claims?* As I view it, in 1984 Congress made a legislative judgment that claims emanating from tainted securities law transactions should not have the same priority as the claims of general creditors of the estate. [emphasis added]
>
> [...]

25. Further, the U.S. courts have held that the degree of culpability of the respective parties is a non-issue in the disallowance of claims for indemnification of underwriters; the equities are meant to benefit the debtor's direct creditors, not secondarily liable creditors with contingent claims.

> *In re Drexel Burnham Lambert Group*, 148 B.R. 982, 1992 Bankr. LEXIS 2023 (Bankr. S.D.N.Y. 1992) [...]

[70] Counsel submits that there is no principled basis for treating indemnification claims of auditors differently than those of underwriters.

Analysis

Is it Premature to Determine the Issue?

[71] The class action litigation was commenced prior to the CCAA Proceedings. It is clear that the claims of shareholders as set out in the class action claims against SFC are "equity claims" within the meaning of the CCAA.

[72] In my view, this issue is not premature for determination, as is submitted by the Underwriters.

[73] The Class Action Proceedings preceded the CCAA Proceedings. It has been clear since the outset of the CCAA Proceedings that this issue – namely, whether the claims of E&Y, BDO and the Underwriters as against SFC, would be considered "equity claims" – would have to be determined.

[74] It has also been clear from the outset of the CCAA Proceedings, that a Sales Process would be undertaken and the expected proceeds arising from the Sales Process would generate proceeds insufficient to satisfy the claims of creditors.

[75] The Claims Procedure is in place but, it seems to me that the issue that has been placed before the court on this motion can be determined independently of the Claims Procedure. I do not accept that any party can be said to be prejudiced if this threshold issue is determined at this time. The threshold issue does not depend upon a determination of quantification of any claim. Rather, its effect will be to establish whether the claims of E&Y, BDO and the Underwriters will be subordinated pursuant to the provisions of the CCAA. This is independent from a determination as to the validity of any claim and the quantification thereof.

Should the Equity Claims Order be Granted?

[76] I am in agreement with the submission of counsel for the Ad Hoc Noteholders to the effect that the characterization of claims for indemnity turns on the characterization of the underlying primary claims.

[77] In my view, the claims advanced in the Shareholder Claims are clearly equity claims. The Shareholder Claims underlie the Related Indemnity Claims.

[78] In my view, the CCAA Amendments have codified the treatment of claims addressed in pre-amendment cases and have further broadened the scope of equity claims.

[79] The plain language in the definition of "equity claim" does not focus on the identity of the claimant. Rather, it focuses on the nature of the claim. In this case, it seems clear that the Shareholder Claims led to the Related Indemnity Claims. Put another way, the inescapable conclusion is that the Related Indemnity Claims are being used to recover an equity investment.

[80] The plain language of the CCAA dictates the outcome, namely, that the Shareholder Claims and the Related Indemnity Claims constitute "equity claims" within the meaning of the CCAA. This conclusion is consistent with the trend towards an expansive interpretation of the definition of "equity claims" to achieve the purpose of the CCAA.

[81] In *Return on Innovation*, Newbould J. characterized the contractual indemnification claims of directors and officers as "equity claims". The Court of Appeal denied leave to appeal. The analysis in *Return on Innovation* leads to the conclusion that the Related Indemnity Claims are also equity claims under the CCAA.

[82] It would be totally inconsistent to arrive at a conclusion that would enable either the auditors or the Underwriters, through a claim for indemnification, to be treated as creditors when the underlying actions of the shareholders cannot achieve the same status. To hold otherwise would indeed provide an indirect remedy where a direct remedy is not available.

[83] Further, on the issue of whether the claims of E&Y, BDO and the Underwriters fall within the definition of equity claims, there are, in my view, two aspects of these claims and it is necessary to keep them conceptually separate.

[84] The first and most significant aspect of the claims of E&Y, BDO and the Underwriters constitutes an "equity claim" within the meaning of the CCAA. Simply put, but for the Class Action Proceedings, it is inconceivable that claims of this magnitude would have been launched by E&Y, BDO and the Underwriters as against SFC. The class action plaintiffs have launched their actions against SFC, the auditors and the Underwriters. In turn, E&Y, BDO and the Underwriters have launched actions against SFC and its subsidiaries. The claims of the shareholders are clearly "equity claims" and a plain reading of s. 2(1)(e) of the CCAA leads to the same conclusion with respect to the claims of E&Y, BDO and the Underwriters. To hold otherwise, would, as stated above, lead to a result that is inconsistent with the principles of the CCAA. It would potentially put the shareholders in a position to achieve creditor status through their claim against E&Y, BDO and the Underwriters even though a direct claim against SFC would rank as an "equity claim".

[85] I also recognize that the legal construction of the claims of the auditors and the Underwriters as against SFC is different than the claims of the shareholders against SFC. However, that distinction is not, in my view, reflected in the language of the CCAA which makes no distinction based on the status of the party but rather focuses on the substance of the claim.

[86] Critical to my analysis of this issue is the statutory language and the fact that the CCAA Amendments came into force after the cases relied upon by the Underwriters and the auditors.

[87] It has been argued that the amendments did nothing more than codify pre-existing common law. In many respects, I accept this submission. However, I am unable to accept this submission when considering s. 2(1) of the CCAA, which provides clear and specific language directing that "equity claim" means a claim that is in respect of an equity interest, including a claim for, among other things, "(e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d)".

[88] Given that a shareholder claim falls within s. 2(1)(d), the plain words of subsections (d) and (e) lead to the conclusions that I have set out above.

[89] I fail to see how the very clear words of subsection (e) can be seen to be a codification of existing law. To arrive at the conclusion put forth by E&Y, BDO and the Underwriters would require me to ignore the specific words that Parliament has recently enacted.

[90] I cannot agree with the position put forth by the Underwriters or by the auditors on this point. The plain wording of the statute has persuaded me that it does not matter whether an indemnity claim is seeking no more than allocation of fault and contribution at common law, or whether there is a free-standing contribution and indemnity claim based on contracts.

[91] However, that is not to say that the full amount of the claim by the auditors and Underwriters can be characterized, at this time, as an "equity claim".

[92] The second aspect to the claims of the auditors and underwriters can be illustrated by the following hypothetical: if the claim of the shareholders does not succeed against the class action defendants, E&Y, BDO and the Underwriters will not be liable to the class action plaintiffs. However, these parties may be in a position to demonstrate that they do have a claim against SFC for the costs of defending those actions, which claim does not arise as a result of "contribution or indemnity in respect of an equity claim".

[93] It could very well be that each of E&Y, BDO and the Underwriters have expended significant amounts in defending the claims brought by the class action plaintiffs which, in turn, could give rise to contractual claims as against SFC. If there is no successful equity claim brought by the class action plaintiffs, it is arguable that any claim of E&Y, BDO and the Underwriters may legitimately be characterized as a claim for contribution or indemnity but not necessarily in respect of an equity claim. If so, there is no principled basis for subordinating this portion of the claim. At this point in time, the quantification of such a claim cannot be determined. This must be determined in accordance with the Claims Procedure.

[94] However, it must be recognized that, by far the most significant part of the claim, is an "equity claim".

[95] In arriving at this determination, I have taken into account the arguments set forth by E&Y, BDO and the Underwriters. My conclusions recognize the separate aspects of the Related Indemnity Claims as submitted by counsel to the Underwriters at paragraph 40 of their factum which reads:

> …it must be recognized that there are, in fact, at least two different kinds of Related Indemnity Claims:
>
> (a) indemnity claims against SFC in respect of Shareholder Claims against the auditors and the Underwriters; and
>
> (b) indemnity claims against SFC in respect of the defence costs of the auditors and the Underwriters in connection with defending themselves against Shareholder Claims.

Disposition

[96] In the result, an order shall issue that the claims against SFC resulting from the ownership, purchase or sale of equity interests in SFC, including, without limitation, the claims by or on behalf of current or former shareholders asserted in the proceedings listed in Schedule "A" are "equity claims" as defined in s. 2 of the CCAA, being claims in respect of monetary losses resulting from the ownership, purchase or sale of an equity interest. It is noted that counsel for the class action plaintiffs did not contest this issue.

[97] In addition, an order shall also issue that any indemnification claim against SFC related to or arising from the Shareholders Claims, including, without limitation, by or on behalf of any of the other defendants to the proceedings listed in Schedule "A" are "equity claims" under the CCAA, being claims for contribution or indemnity in respect of a claim that is an equity claim. However, I feel it is premature to determine whether this order extends to the aspect of the Related Indemnity Claims that corresponds to the defence costs of the Underwriters and the auditors in connection with defending themselves against the Shareholder Claims.

[98] A direction shall also issue that these orders are made without prejudice to SFC's rights to apply for a similar order with respect to (i) any claims in the statement of claim that are in respect of securities other than shares and (ii) any indemnification claims against SFC related thereto.

MORAWETZ J.

Date: July 27, 2012

SCHEDULE "A" – SHAREHOLDER CLAIMS

1. *Trustees of the Labourers' Pension Fund of Central and Eastern Canada et al. v. Sino-Forest Corporation et al.* (Ontario Superior Court of Justice, Court File No. CV-11-431153-00CP)

2. *Guining Liu v. Sino-Forest Corporation et al.* (Quebec Superior Court, Court File No.: 200-06-000132-111)

3. *Allan Haigh v. Sino-Forest Corporation et al.* (Saskatchewan Court of Queen's Bench, Court File No. 2288 of 2011)

4. *David Leapard et al. v. Allen T.Y. Chan et al.* (District court of the Southern District of New York, Court File No. 650258/2012)

TAB 16

In the Matter of a Plan of Compromise or Arrangement of
Sino-Forest Corporation

[Indexed as: Sino-Forest Corp. (Re)]

114 O.R. (3d) 304

2012 ONCA 816

Court of Appeal for Ontario,
Goudge, Hoy and Pepall JJ.A.
November 23, 2012

Debtor and creditor -- Arrangements -- Shareholders of company commencing class actions against company, underwriters and auditors for misrepresentation -- Plaintiffs alleging that misrepresentations artificially inflated price of company's shares -- Company successfully seeking protection under Companies' Creditors Arrangement Act ("CCAA") -- Underwriters and auditors filing proofs of claim against company seeking contribution and indemnity for any amounts they might be ordered to pay as damages in class actions -- Supervising judge not erring in finding that those claims were equity claims within meaning of s. 2(1) of CCAA despite fact that underwriters and auditors were not holders of an equity interest -- Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, s. 2(1).

The appellant underwriters provided underwriting services in connection with three S Co. equity offerings and four S Co. note offerings. The appellant auditors served as S Co.'s auditors at the relevant time. Shareholders of S Co. brought

proposed class actions against S Co. and, among others, the underwriters and auditors, alleging that S Co. repeatedly misrepresented its assets and financial situation and its compliance with generally accepted accounting principles in its public disclosure, that the auditors and underwriters failed to detect those misrepresentations, and that the auditors misrepresented that their audit reports [page305] were prepared in accordance with generally accepted auditing standards. They claimed that the misrepresentations artificially inflated the price of S Co.'s shares and that proposed class members suffered damages when the shares fell after the truth was revealed. S Co. successfully sought protection pursuant to the provisions of the Companies' Creditors Arrangement Act ("CCAA"). The auditors and underwriters filed proofs of claim seeking contribution and indemnity for, among other things, any amounts that they were ordered to pay as damages to the plaintiffs in the class actions. S Co. applied for an order that the claims against it arising from the ownership, purchase or sale of an equity interest in the company, including shareholder claims, and any indemnification claim against it related to or arising from the shareholder claims, including the claims for contribution or indemnity, were equity claims under the CCAA. The application was granted. The underwriters and auditors appealed.

Held, the appeal should be dismissed.

The definition of equity claim in s. 2(1) of the CCAA focuses on the nature of the claim, and not the identity of the claimant. The appellants' claims for contribution and indemnity were clearly equity claims, despite the fact that the appellants did not have an equity interest in S Co. Parliament adopted expansive language in defining "equity claim". Parliament employed the phrase "in respect of" twice in defining equity claim: in the opening portion of the definition, it refers to an equity claim as a "claim that is in respect of an equity interest", and in para. (e) it refers to "contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d)". The Supreme Court of Canada has repeatedly held that the words "in respect of" are of the widest possible scope, conveying some link or connection

between two related subjects. It was conceded that the shareholder claims against S Co. were claims for "a monetary loss resulting from the ownership, purchase or sale of an equity interest", within the meaning of para. (d) of the definition of "equity claim". There was an obvious link between the appellants' claims against S Co. for contribution and indemnity and the shareholders' claims against S Co. Parliament also defined equity claim as "including a claim for, among others", the claims described in paras. (a) to (e). The Supreme Court has held that the phrase "including" indicates that the preceding words -- "a claim that is in respect of an equity interest" -- should be given an expansive interpretation, and include matters which might not otherwise be within the meaning of the term. Accordingly, the appellants' claims, which clearly fell within para. (e), were included within the meaning of the phrase "claim that is in respect of an equity interest". Parliament chose not to include language in s. 2(1) restricting claims for contribution or indemnity to those made by shareholders. If only a person with an equity interest could assert an equity claim, para. (e) would be rendered meaningless. No legislative provision should be interpreted so as to render it mere surplusage. Looking at s. 2(1) as a whole, it appeared that the remedies available to shareholders were all addressed by s. 2(1)(a) to (d). The logic of s. 2(1)(a) to (e) therefore also supported the notion that para. (e) referred to claims for contribution and indemnity not by shareholders, but by others. The definition of "equity claim" was sufficiently clear to alter the pre-existing common law.

Cases referred to

Blue Range Resource Corp. (Re), [2000] A.J. No. 14, 2000 ABQB 4, [2000] 4 W.W.R. 738, 76 Alta. L.R. (3d) 338, 259 A.R. 30, 15 C.B.R. (4th) 169, 94 A.C.W.S. (3d) 223; CanadianOxy Chemicals Ltd. v. Canada (Attorney General), [1999] 1 S.C.R. 743, [1998] S.C.J. No. 87, 171 D.L.R. (4th) 733, 237 N.R. 373, J.E. 99-861, 122 B.C.A.C. 1, 133 C.C.C. (3d) 426, 29 C.E.L.R. (N.S.) 1, 23 C.R. (5th) 259, 41 W.C.B. (2d) 411; [page306] Central Capital Corp. (Re) (1996), 27 O.R. (3d) 494, [1996] O.J. No. 359, 132 D.L.R. (4th) 223, 88 O.A.C. 161, 26 B.L.R. (2d) 88, 38 C.B.R. (3d) 1, 61 A.C.W.S. (3d) 18 (C.A.); EarthFirst Canada Inc. (Re), [2009] A.J. No. 749, 2009 ABQB 316, 56 C.B.R. (5th) 102; Goodyear Tire & Rubber

Co. of Canada v. T. Eaton Co., [1956] S.C.R. 610, [1956] S.C.J. No. 37, 4 D.L.R. (2d) 1, 28 C.P.R. 25, 56 D.T.C. 1060; In Re: Mid-American Waste Systems, Inc., 228 B.R. 816 (Bankr. Del. 1999); Markevich v. Canada, [2003] 1 S.C.R. 94, [2003] S.C.J. No. 8, 2003 SCC 9, 239 F.T.R. 159, 223 D.L.R. (4th) 17, 300 N.R. 321, J.E. 2003-506, 2003 D.T.C. 5185, 120 A.C.W.S. (3d) 532; National Bank of Canada v. Merit Energy Ltd., [2002] A.J. No. 6, 2002 ABCA 5, [2002] 3 W.W.R. 215, 317 A.R. 319, affg [2001] A.J. No. 918, 2001 ABQB 583, [2001] 10 W.W.R. 305, 95 Alta. L.R. (3d) 166, 294 A.R. 15, 28 C.B.R. (4th) 228, 107 A.C.W.S. (3d) 182 (Q.B.); National Bank of Greece (Canada) v. Katsikonouris, [1990] 2 S.C.R. 1029, [1990] S.C.J. No. 95, 74 D.L.R. (4th) 197, 115 N.R. 42, J.E. 90-1410, 32 Q.A.C. 250, 50 C.C.L.I. 1, [1990] I.L.R. 1-2663 at 10478, 23 A.C.W.S. (3d) 74; Nelson Financial Group Ltd. (Re), [2010] O.J. No. 4903, 2010 ONSC 6229, 75 B.L.R. (4th) 302, 71 C.B.R. (5th) 153 (S.C.J.); Parry Sound (District) Social Services Administration Board v. Ontario Public Service Employees Union, Local 324, [2003] 2 S.C.R. 157, [2003] S.C.J. No. 42, 2003 SCC 42, 230 D.L.R. (4th) 257, 308 N.R. 271, 177 O.A.C. 235, J.E. 2003-1790, 7 Admin. L.R. (4th) 177, 31 C.C.E.L. (3d) 1, [2003] CLLC 220-062, 125 A.C.W.S. (3d) 85; R. v. Nowegijick, [1983] 1 S.C.R. 29, [1983] S.C.J. No. 5, 144 D.L.R. (3d) 193, 46 N.R. 41, [1983] 2 C.N.L.R. 89, [1983] C.T.C. 20, 83 D.T.C. 5041, 18 A.C.W.S. (2d) 2; R. v. Proulx, [2000] 1 S.C.R. 61, [2000] S.C.J. No. 6, 2000 SCC 5, 182 D.L.R. (4th) 1, 249 N.R. 201, [2000] 4 W.W.R. 21, J.E. 2000-264, 142 Man. R. (2d) 161, 140 C.C.C. (3d) 449, 30 C.R. (5th) 1, 49 M.V.R. (3d) 163, 44 W.C.B. (2d) 479; Return on Innovation Capital Ltd. v. Gandi Innovations Ltd., [2011] O.J. No. 3827, 2011 ONSC 5018, 83 C.B.R. (5th) 123, 206 A.C.W.S. (3d) 464 (S.C.J.) [Leave to appeal refused [2012] O.J. No. 31, 2012 ONCA 10, 90 C.B.R. (5th) 141, 211 A.C.W.S. (3d) 264]; Stelco Inc. (Re), [2006] O.J. No. 276, 14 B.L.R. (4th) 260, 17 C.B.R. (5th) 78, 145 A.C.W.S. (3d) 194 (S.C.J.)

Statutes referred to

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 2 [as am.], 121 [as am.]

Bankruptcy Code, 11 U.S.C.S. 502(e)(1)(B)

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

am.], ss. 2(1) [as am], (a)-(e), 6(8), 22.1 [as am.]
Negligence Act, R.S.O. 1990, c. N.1 [as am.], s. 2
Securities Act, R.S.A. 2000, c. S-4, s. 203(1) [as am.], (10)
Securities Act, R.S.B.C. 1996, c. 418, s. 131(1) [as am.], (11)
Securities Act, R.S.N.L. 1990, c. S-13, s. 130(1), (8)
Securities Act, R.S.N.S. 1989, c. 418, s. 137(1), (8)
Securities Act, R.S.O. 1990, c. S.5, s. 130(1) [as am.], (8)
Securities Act, R.S.P.E.I. 1988, c. S-3.1, s. 111(1), (12)
Securities Act, R.S.Q., c. V-1.1, ss. 218 [as am.], 219, 221 [as am.]
Securities Act, S.N.B. 2004, c. S-5.5, s. 149(1), (9)
Securities Act, S.N.W.T. 2008, c. 10, s. 111(1), (12)
Securities Act, S.Nu. 2008, c. 12, s. 111(1), (12)
Securities Act, S.Y. 2007, c. 16, s. 111(1), (13)
The Securities Act, C.C.S.M. c. S50, s. 141(1), (11)
The Securities Act, 1988, S.S. 1988-89, c. S-42.2, s. 137(1), (9)
Authorities referred to
Driedger, Elmer A., Construction of Statutes, 2nd ed. (Toronto: Butterworths, 1983) [page307]

APPEAL from the order of Morawetz J., [2012] O.J. No. 3627, 2012 ONSC 4377 (S.C.J.) declaring that the appellants' claims were equity claims within the meaning of the Companies' Creditors Arrangement Act.

Peter H. Griffin, Peter J. Osborne and Shara Roy, for appellant Ernst & Young LLP.

Sheila Block and David Bish, for appellants Credit Suisse Securities (Canada) Inc., TD Securities Inc., Dundee Securities Corporation (now known as DWM Securities Inc.), RBC Dominion Securities Inc., Scotia Capital Inc., CIBC World Markets Inc., Merrill Lynch Canada Inc., Canaccord Financial Ltd. (now known as Canaccord Genuity Corp.), Maison Placements Canada Inc., Credit Suisse Securities (USA) LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated, successor by merger to Banc of America Securities LLC.

Kenneth Dekker, for appellant BDO Limited.

Robert W. Staley, Derek J. Bell and Jonathan Bell, for respondent Sino-Forest Corporation.

Benjamin Zarnett, Robert Chadwick and Julie Rosenthal, for respondent Ad Hoc Committee of Noteholders.

Clifton Prophet, for monitor FTI Consulting Canada Inc.

Kirk M. Baert, A. Dimitri Lascaris and Massimo Starnino, for respondent Ad Hoc Committee of Purchasers.

Emily Cole, for respondent Allen Chan.

Erin Pleet, for respondent David Horsley.

David Gadsden, for respondent Pyry (Beijing).

Larry Lowenstein and Edward A. Sellers, for respondent board of directors.

BY THE COURT: --

I Overview

[1] In 2009, the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended ("CCAA"), was amended to expressly provide that general creditors are to be paid in full before an equity claim is paid.

[2] This appeal considers the definition of "equity claim" in s. 2(1) of the CCAA. More particularly, the central issue is whether claims by auditors and underwriters against the respondent debtor, Sino-Forest Corporation ("Sino-Forest"), for contribution and indemnity fall within that definition. The claims arise out of proposed shareholder class actions for misrepresentation. [page308]

[3] The appellants argue that the supervising judge erred in concluding that the claims at issue are equity claims within

the meaning of the CCAA and in determining the issue before the claims procedure established in Sino-Forest's CCAA proceeding had been completed.

[4] For the reasons that follow, we conclude that the supervising judge did not err and accordingly dismiss this appeal.

II The Background

(a) The parties

[5] Sino-Forest is a Canadian public holding company that holds the shares of numerous subsidiaries, which in turn own, directly or indirectly, forestry assets located principally in the People's Republic of China. Its common shares are listed on the Toronto Stock Exchange. Sino-Forest also issued approximately $1.8 billion of unsecured notes, in four series. Trading in Sino-Forest shares ceased on August 26, 2011, as a result of a cease-trade order made by the Ontario Securities Commission.

[6] The appellant underwriters [See Note 1 below] provided underwriting services in connection with three separate Sino-Forest equity offerings in June 2007, June 2009 and December 2009, and four separate Sino-Forest note offerings in July 2008, June 2009, December 2009 and October 2010. Certain underwriters entered into agreements with Sino-Forest in which Sino-Forest agreed to indemnify the underwriters in connection with an array of matters that could arise from their participation in these offerings.

[7] The appellant BDO Limited ("BDO") is a Hong Kong-based accounting firm that served as Sino-Forest's auditor between 2005 and August 2007, and audited its annual financial statements for the years ended December 31, 2005 and December 31, 2006.

[8] The engagement agreements governing BDO's audits of Sino-Forest provided that the company's management bore the primary responsibility for preparing its financial statements in accordance with generally accepted accounting principles ("GAAP") [page309] and implementing internal controls to

prevent and detect fraud and error in relation to its financial reporting.

[9] BDO's audit report for 2006 was incorporated by reference into a June 2007 prospectus issued by Sino-Forest regarding the offering of its shares to the public. This use by Sino-Forest was governed by an engagement agreement dated May 23, 2007 in which Sino-Forest agreed to indemnify BDO in respect of any claims by the underwriters or any third party that arose as a result of the further steps taken by BDO in relation to the issuance of the June 2007 prospectus.

[10] The appellant Ernst & Young LLP ("E&Y") served as Sino-Forest's auditor for the years 2007 to 2012, and delivered auditors' reports with respect to the consolidated financial statements of Sino-Forest for fiscal years ended December 31, 2007 to 2010, inclusive. In each year for which it prepared a report, E&Y entered into an audit engagement letter with Sino-Forest in which Sino-Forest undertook to prepare its financial statements in accordance with GAAP, design and implement internal controls to prevent and detect fraud and error, and provide E&Y with its complete financial records and related information. Some of these letters contained an indemnity in favour of E&Y.

[11] The respondent Ad Hoc Committee of Noteholders consists of noteholders owning approximately one-half of Sino-Forest's total noteholder debt. [See Note 2 below] They are creditors who have debt claims against Sino-Forest; they are not equity claimants.

[12] Sino-Forest has insufficient assets to satisfy all the claims against it. To the extent that the appellants' claims are accepted and are treated as debt claims rather than equity claims, the noteholders' recovery will be diminished.

(b) The class actions

[13] In 2011 and January of 2012, proposed class actions were commenced in Ontario, Quebec, Saskatchewan and New York State against, amongst others, Sino-Forest, certain of its officers, directors and employees, BDO, E&Y and the underwriters. Sino-

Forest is sued in all actions. [See Note 3 below] [page310]

[14] The proposed representative plaintiffs in the class actions are shareholders of Sino-Forest. They allege that Sino-Forest repeatedly misrepresented its assets and financial situation and its compliance with GAAP in its public disclosure; the appellant auditors and underwriters failed to detect these misrepresentations; and the appellant auditors misrepresented that their audit reports were prepared in accordance with generally accepted auditing standards ("GAAS"). The representative plaintiffs claim that these misrepresentations artificially inflated the price of Sino-Forest's shares and that proposed class members suffered damages when the shares fell after the truth was revealed in 2011.

[15] The representative plaintiffs in the Ontario class action seek approximately $9.2 billion in damages. The Quebec, Saskatchewan and New York class actions do not specify the quantum of damages sought.

[16] To date, none of the proposed class actions has been certified.

(c) CCAA protection and proofs of claim

[17] On March 30, 2012, Sino-Forest sought protection pursuant to the provisions of the CCAA. Morawetz J. granted the initial order which, among other things, appointed FTI Consulting Canada Inc. as the monitor and stayed the class actions as against Sino-Forest. Since that time, Morawetz J. has been the supervising judge of the CCAA proceedings. The initial stay of the class actions was extended and broadened by order dated May 8, 2012.

[18] On May 14, 2012, the supervising judge granted an unopposed claims procedure order which established a procedure to file and determine claims against Sino-Forest.

[19] Thereafter, all of the appellants filed individual proofs of claim against Sino-Forest seeking contribution and indemnity for, among other things, any amounts that they are

ordered to pay as damages to the plaintiffs in the class actions. Their proofs of claim advance several different legal bases for Sino-Forest's alleged obligation of contribution and indemnity, including breach of contract, contractual terms of indemnity, negligent and fraudulent misrepresentation in tort, and the provisions of the Negligence Act, R.S.O. 1990, c. N.1.

(d) Order under appeal

[20] Sino-Forest then applied for an order that the following claims are equity claims under the CCAA: claims against Sino-Forest arising from the ownership, purchase or sale of an equity [page311] interest in the company, including shareholder claims ("shareholder claims"); and any indemnification claims against Sino-Forest related to or arising from the shareholder claims, including the appellants' claims for contribution or indemnity ("related indemnity claims").

[21] The motion was supported by the Ad Hoc Committee of Noteholders.

[22] On July 27, 2012, the supervising judge granted the order sought by Sino-Forest and released a comprehensive endorsement.

[23] He concluded that it was not premature to determine the equity claims issue. It had been clear from the outset of Sino-Forest's CCAA proceedings that this issue would have to be decided and that the expected proceeds arising from any sales process would be insufficient to satisfy the claims of creditors. Furthermore, the issue could be determined independently of the claims procedure and without prejudice being suffered by any party.

[24] He also concluded that both the shareholder claims and the related indemnity claims should be characterized as equity claims. In summary, he reasoned that

-- the characterization of claims for indemnity turns on the characterization of the underlying primary claims. The shareholder claims are clearly equity claims and they led to and underlie the related indemnity claims;
-- the plain language of the CCAA, which focuses on the nature

of the claim rather than the identity of the claimant, dictates that both shareholder claims and related indemnity claims constitute equity claims;

-- the definition of "equity claim" added to the CCAA in 2009 broadened the scope of equity claims established by pre-amendment jurisprudence;

-- this holding is consistent with the analysis in Return on Innovation Capital Ltd. v. Gandi Innovations Ltd., [2011] O.J. No. 3827, 2011 ONSC 5018, 83 C.B.R. (5th) 123 (S.C.J.), which dealt with contractual indemnification claims of officers and directors. Leave to appeal was denied by this court, [2012] O.J. No. 31, 2012 ONCA 10, 90 C.B.R. (5th) 141; and

-- "[i]t would be totally inconsistent to arrive at a conclusion that would enable either the auditors or the underwriters, through a claim for indemnification, to be treated as creditors [page312] when the underlying actions of shareholders cannot achieve the same status" (para. 82). To hold otherwise would run counter to the scheme established by the CCAA and would permit an indirect remedy to the shareholders when a direct remedy is unavailable.

[25] The supervising judge did not characterize the full amount of the claims of the auditors and underwriters as equity claims. He excluded the claims for defence costs on the basis that while it was arguable that they constituted claims for indemnity, they were not necessarily in respect of an equity claim. That determination is not appealed.

III Interpretation of "Equity Claim"

(a) Relevant statutory provisions

[26] As part of a broad reform of Canadian insolvency legislation, various amendments to the CCAA were proclaimed in force as of September 18, 2009.

[27] They included the addition of s. 6(8):

> 6(8) No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

Section 22.1, which provides that creditors with equity claims may not vote at any meeting unless the court orders otherwise, was also added.

[28] Related definitions of "claim", "equity claim" and "equity interest" were added to s. 2(1) of the CCAA:

> 2(1) In this Act,
>
> . . . . .
>
> "claim" means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the Bankruptcy and Insolvency Act;
>
> . . . . .
>
> "equity claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
>
> (b) a return of capital,
>
> (c) a redemption or retraction obligation, [page313]
>
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
>
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);
>
> "equity interest" means
>
> (a) in the case of a company other than an income trust, a share in the company -- or a warrant or option or another right to acquire a share in the company -- other than one that is derived from a convertible debt, and
>
> (b) in the case of an income trust, a unit in the income trust -- or a warrant or option or another right to acquire a unit in the income trust -- other than one that is derived from a convertible debt[.]

(Emphasis added)

[29] Section 2 of the Bankruptcy and Insolvency Act, R.S.C.

1985, c. B-3 ("BIA") defines a "claim provable in bankruptcy". Section 121 of the BIA in turn specifies that claims provable in bankruptcy are those to which the bankrupt is subject.

> 2. "claim provable in bankruptcy", "provable claim" or "claim provable" includes any claim or liability provable in proceedings under this Act by a creditor;
>
> . . . . .
>
> 121(1) All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt or to which the bankrupt may become subject before the bankrupt's discharge by reason of any obligation incurred before the day on which the bankrupt becomes bankrupt shall be deemed to be claims provable in proceedings under this Act.

(Emphasis added)

(b) The legal framework before the 2009 amendments

[30] Even before the 2009 amendments to the CCAA codified the treatment of equity claims, the courts subordinated shareholder equity claims to general creditors' claims in an insolvency. As the supervising judge described [at paras. 23-25]:

> Essentially, shareholders cannot reasonably expect to maintain a financial interest in an insolvent company where creditor claims are not being paid in full. Simply put, shareholders have no economic interest in an insolvent enterprise.
>
> The basis for the differentiation flows from the fundamentally different nature of debt and equity investments. Shareholders have unlimited upside potential when purchasing shares. Creditors have no corresponding upside potential. [page314]
>
> As a result, courts subordinated equity claims and denied such claims a vote in plans of arrangement.

(Citations omitted) [See Note 4 below]

(c) The appellants' submissions

[31] The appellants essentially advance three arguments.

[32] First, they argue that on a plain reading of s. 2(1), their claims are excluded. They focus on the opening words of the definition of "equity claim" and argue that their claims against Sino-Forest are not claims that are "in respect of an equity interest" because they do not have an equity interest in Sino-Forest. Their relationships with Sino-Forest were purely contractual and they were arm's-length creditors, not shareholders with the risks and rewards attendant to that position. The policy rationale behind ranking shareholders below creditors is not furthered by characterizing the appellants' claims as equity claims. They were service providers with a contractual right to an indemnity from Sino-Forest.

[33] Second, the appellants focus on the term "claim" in para. (e) of the definition of "equity claim", and argue that the claims in respect of which they seek contribution and indemnity are the shareholders' claims against them in court proceedings for damages, which are not "claims" against Sino-Forest provable within the meaning of the BIA and, therefore, not "claims" within s. 2(1). They submit that the supervising judge erred in focusing on the characterization of the underlying primary claims.

[34] Third, the appellants submit that the definition of "equity claim" is not sufficiently clear to have changed the existing law. It is assumed that the legislature does not intend to change the common law without "expressing its intentions to do so with irresistible clearness": Parry Sound (District) Social Services Administration Board v. Ontario Public Service Employees Union, Local 324, [2003] 2 S.C.R. 157, [2003] S.C.J. No. 42, 2003 SCC 42, at para. 39, citing Goodyear Tire & Rubber Co. of Canada v. T. Eaton Co., [1956] S.C.R. 610, [1956] S.C.J. No. 37, at p. 614 S.C.R. The appellants argue that the supervising judge's interpretation of "equity claim" dramatically alters the common [page315] law as reflected in National Bank of Canada v. Merit Energy Ltd., [2001] A.J. No. 918, 2001 ABQB 583, 294 A.R. 15, affd [2002] A.J. No. 6, 2002 ABCA 5, 317 A.R. 319. There, the court

determined that in an insolvency, claims of auditors and underwriters for indemnification are not to be treated in the same manner as claims by shareholders. Furthermore, the Senate debates that preceded the enactment of the amendments did not specifically comment on the effect of the amendments on claims by auditors and underwriters. The amendments should be interpreted as codifying the pre-existing common law as reflected in National Bank of Canada v. Merit Energy Ltd.

[35] The appellants argue that the decision of Return on Innovation Capital Ltd. v. Gandi Innovations Ltd. is distinguishable because it dealt with the characterization of claims for damages by an equity investor against officers and directors, and it predated the 2009 amendments. In any event, this court confirmed that its decision denying leave to appeal should not be read as a judicial precedent for the interpretation of the meaning of "equity claim" in s. 2(1) of the CCAA.

(d) Analysis

(i) Introduction

[36] The exercise before this court is one of statutory interpretation. We are therefore guided by the following oft-cited principle from Elmer A. Driedger, Construction of Statutes, 2nd ed. (Toronto: Butterworths, 1983), at p. 87:

> [T]he words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament.

[37] We agree with the supervising judge that the definition of equity claim focuses on the nature of the claim, and not the identity of the claimant. In our view, the appellants' claims for contribution and indemnity are clearly equity claims.

[38] The appellants' arguments do not give effect to the expansive language adopted by Parliament in defining "equity claim" and read in language not incorporated by Parliament. Their interpretation would render para. (e) of the definition meaningless and defies the logic of the section.

(ii) The expansive language used

[39] The definition incorporates two expansive terms.

[40] First, Parliament employed the phrase "in respect of" twice in defining equity claim: in the opening portion of the definition, it refers to an equity claim as a "claim that is in respect of [page316] an equity interest", and in para. (e) it refers to "contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d)" (emphasis added).

[41] The Supreme Court of Canada has repeatedly held that the words "in respect of" are "of the widest possible scope", conveying some link or connection between two related subjects. In CanadianOxy Chemicals Ltd. v. Canada (Attorney General), [1999] 1 S.C.R. 743, [1998] S.C.J. No. 87, at para. 16, citing R. v. Nowegijick, [1983] 1 S.C.R. 29, [1983] S.C.J. No. 5, at p. 39 S.C.R., the Supreme Court held as follows:

> The words "in respect of" are, in my opinion, words of the widest possible scope. They import such meanings as "in relation to", "with reference to" or "in connection with". The phrase "in respect of" is probably the widest of any expression intended to convey some connection between two related subject matters.

(Emphasis added in CanadianOxy)

That court also stated as follows in Markevich v. Canada, [2003] 1 S.C.R. 94, [2003] S.C.J. No. 8, 2003 SCC 9, at para. 26:

> The words "in respect of" have been held by this Court to be words of the broadest scope that convey some link between two subject matters.

(Citations omitted)

[42] It is conceded that the shareholder claims against Sino-Forest are claims for "a monetary loss resulting from the ownership, purchase or sale of an equity interest", within the meaning of para. (d) of the definition of "equity claim". There is an obvious link between the appellants' claims against Sino-Forest for contribution and indemnity and the shareholders'

claims against Sino-Forest. The legal proceedings brought by the shareholders asserted their claims against Sino-Forest together with their claims against the appellants, which gave rise to these claims for contribution and indemnity. The causes of action asserted depend largely on common facts and seek recovery of the same loss.

[43] The appellants' claims for contribution or indemnity against Sino-Forest are therefore clearly connected to or "in respect of" a claim referred to in para. (d), namely, the shareholders' claims against Sino-Forest. They are claims in respect of equity claims by shareholders and are provable in bankruptcy against Sino-Forest.

[44] Second, Parliament also defined equity claim as "including a claim for, among others", the claims described in paras. (a) to (e). The Supreme Court has held that this phrase "including" indicates that the preceding words -- "a claim that is in respect of an equity interest" -- should be given an expansive [page317] interpretation, and include matters which might not otherwise be within the meaning of the term, as stated in National Bank of Greece (Canada) v. Katsikonouris, [1990] 2 S.C.R. 1029, [1990] S.C.J. No. 95, at p. 1041 S.C.R.:

> [T]hese words are terms of extension, designed to enlarge the meaning of preceding words, and not to limit them.
>
> [T]he natural inference is that the drafter will provide a specific illustration of a subset of a given category of things in order to make it clear that that category extends to things that might otherwise be expected to fall outside it.

[45] Accordingly, the appellants' claims, which clearly fall within para. (e), are included within the meaning of the phrase a "claim that is in respect of an equity interest".

(iii) What Parliament did not say

[46] "Equity claim" is not confined by its definition, or by the definition of "claim", to a claim advanced by the holder of

an equity interest. Parliament could have, but did not, include language in para. (e) restricting claims for contribution or indemnity to those made by shareholders.

(iv) An interpretation that avoids surplusage

[47] A claim for contribution arises when the claimant for contribution has been sued. Section 2 of the Negligence Act provides that a tortfeasor may recover contribution or indemnity from any other tortfeasor who is, or would if sued have been, liable in respect of the damage to any person suffering damage as a result of a tort. The securities legislation of the various provinces provides that an issuer, its underwriters and, if they consented to the disclosure of information in the prospectus, its auditors, among others, are jointly and severally liable for a misrepresentation in the prospectus, and provides for rights of contribution. [See Note 5 below] [page318]

[48] Counsel for the appellants were unable to provide a satisfactory example of when a holder of an equity interest in a debtor company would seek contribution under para. (e) against the debtor in respect of a claim referred to in any of paras. (a) to (d). In our view, this indicates that para. (e) was drafted with claims for contribution or indemnity by non-shareholders rather than shareholders in mind.

[49] If the appellants' interpretation prevailed, and only a person with an equity interest could assert such a claim, para. (e) would be rendered meaningless, and as Lamer C.J.C. wrote in R. v. Proulx, [2000] 1 S.C.R. 61, [2000] S.C.J. No. 6, 2000 SCC 5, at para. 28:

> It is a well accepted principle of statutory interpretation that no legislative provision should be interpreted so as to render it mere surplusage.

(v) The scheme and logic of the section

[50] Moreover, looking at s. 2(1) as a whole, it would appear that the remedies available to shareholders are all addressed by s. 2(1)(a) to (d). The logic of s. 2(1)(a) to (e) therefore also supports the notion that para. (e) refers to claims for

contribution or indemnity not by shareholders, but by others.

(vi) The legislative history of the 2009 amendments

[51] The appellants and the respondents each argue that the legislative history of the amendments supports their respective interpretation of the term "equity claim". We have carefully considered the legislative history. The limited commentary is brief and imprecise. The clause-by-clause analysis of Bill C-12 comments that "[a]n equity claim is defined to include any claim that is related to an equity interest". [See Note 6 below] While, as the appellants submit, there was no specific reference to the position of auditors and underwriters, the desirability of greater conformity with United States insolvency law to avoid forum shopping by debtors was highlighted in 2003, some four years before the definition of "equity claim" was included in Bill C-12.

[52] In this instance, the legislative history ultimately provided very little insight into the intended meaning of the amendments. We have been guided by the plain words used by Parliament in reaching our conclusion. [page319]

(vii) Intent to change the common law

[53] In our view, the definition of "equity claim" is sufficiently clear to alter the pre-existing common law. National Bank of Canada v. Merit Energy Ltd., an Alberta decision, was the single case referred to by the appellants that addressed the treatment of auditors' and underwriters' claims for contribution and indemnity in an insolvency before the definition was enacted. As the supervising judge noted, in a more recent decision, Return on Innovation Capital Ltd. v. Gandi Innovations Ltd., the courts of this province adopted a more expansive approach, holding that contractual indemnification claims of directors and officers were equity claims.

[54] We are not persuaded that the practical effect of the change to the law implemented by the enactment of the definition of "equity claim" is as dramatic as the appellants suggest. The operations of many auditors and underwriters extend to the United States, where contingent claims for

reimbursement or contribution by entities "liable with the debtor" are disallowed pursuant to 502(e)(1)(B) of the U.S. Bankruptcy Code, 11 U.S.C.S. [See Note 7 below]

(viii) The purpose of the legislation

[55] The supervising judge indicated that if the claims of auditors and underwriters for contribution and indemnity were not included within the meaning of "equity claim", the CCAA would permit an indirect remedy to the shareholders when a direct remedy is not available. We would express this concept differently.

[56] In our view, in enacting s. 6(8) of the CCAA, Parliament intended that a monetary loss suffered by a shareholder (or other holder of an equity interest) in respect of his or her equity interest not diminish the assets of the debtor available to general creditors in a restructuring. If a shareholder sues auditors and underwriters in respect of his or her loss, in addition to the debtor, and the auditors or underwriters assert claims of contribution or indemnity against the debtor, the assets of the debtor available to general creditors would be diminished by the amount of the claims for contribution and indemnity. [page320]

IV Prematurity

[57] We are not persuaded that the supervising judge erred by determining that the appellants' claims were equity claims before the claims procedure established in Sino-Forest's CCAA proceeding had been completed.

[58] The supervising judge noted, at para. 7 of his endorsement, that from the outset, Sino-Forest, supported by the monitor, had taken the position that it was important that these proceedings be completed as soon as possible. The need to address the characterization of the appellants' claims had also been clear from the outset. The appellants have not identified any prejudice that arises from the determination of the issue at this stage. There was no additional information that the appellants have identified that was not before the supervising judge. The monitor, a court-appointed officer, supported the motion procedure. The supervising judge was well positioned to

determine whether the procedure proposed was premature and, in our view, there is no basis on which to interfere with the exercise of his discretion.

V Summary

[59] In conclusion, we agree with the supervising judge that the appellants' claims for contribution or indemnity are equity claims within s. 2(1)(e) of the CCAA.

[60] We reach this conclusion because of what we have said about the expansive language used by Parliament, the language Parliament did not use, the avoidance of surplusage, the logic of the section and what, from the foregoing, we conclude is the purpose of the 2009 amendments as they relate to these proceedings.

[61] We see no basis to interfere with the supervising judge's decision to consider whether the appellants' claims were equity claims before the completion of the claims procedure.

VI Disposition

[62] This appeal is accordingly dismissed. As agreed, there will be no costs.

Appeal dismissed.

Notes

Note 1: Credit Suisse Securities (Canada) Inc., TD Securities Inc., Dundee Securities Corporation (now known as DWM Securities Inc.), RBC Dominion Securities Inc., Scotia Capital Inc., CIBC World Markets Inc., Merrill Lynch Canada Inc., Canaccord Financial Ltd. (now known as Canaccord Genuity Corp.), Maison Placements Canada Inc., Credit Suisse Securities (USA) LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated, successor by merger to Banc of America Securities LLC.

Note 2: Noteholders holding in excess of $1.296 billion, or 72 per cent, of Sino-Forest's approximately $1.8 billion in noteholders' debt have executed written support agreements in favour of the Sino-Forest CCAA plan as of March 30, 2012. These include noteholders represented by the Ad Hoc Committee of Noteholders.

Note 3: None of the appellants are sued in Saskatchewan and all are sued in Ontario. E&Y is also sued in Quebec and New York and the appellant underwriters are also sued in New York.

Note 4: The supervising judge cited the following cases as authority for these propositions: Blue Range Resource Corp., (Re), [2000] A.J. No. 14, 2000 ABQB 4, 259 A.R. 30; Stelco Inc. (Re), [2006] O.J. No. 276, 17 C.B.R. (5th) 78 (S.C.J.); Central Capital Corp. (Re) (1996), 27 O.R. (3d) 494, [1996] O.J. No. 359 (C.A.); Nelson Financial Group Ltd. (Re), [2010] O.J. No. 4903, 2010 ONSC 6229, 71 C.B.R. (5th) 153 (S.C.J.); EarthFirst Canada Inc. (Re), [2009] A.J. No. 749, 2009 ABQB 316, 56 C.B.R. (5th) 102.

Note 5: Securities Act, R.S.O. 1990, c. S.5, s. 130(1), (8); Securities Act, R.S.A. 2000, c. S-4, s. 203(1), (10); Securities Act, R.S.B.C. 1996, c. 418, s. 131(1), (11); The Securities Act, C.C.S.M. c. S50, s. 141(1), (11); Securities Act, S.N.B. 2004, c. S-5.5, s. 149(1), (9); Securities Act, R.S.N.L. 1990, c. S-13, s. 130(1), (8); Securities Act, R.S.N.S. 1989, c. 418, s. 137(1), (8); Securities Act, S.Nu. 2008, c. 12, s. 111(1), (12); Securities Act, S.N.W.T. 2008, c. 10, s. 111(1), (12); Securities Act, R.S.P.E.I. 1988, c. S-3.1, s. 111(1), (12); Securities Act, R.S.Q., c. V-1.1, ss. 218, 219, 221; The Securities Act, 1988, S.S. 1988-89, c. S-42.2, s. 137(1), (9); Securities Act, S.Y. 2007, c. 16, s. 111(1), (13).

Note 6: We understand that this analysis was before the Standing Senate Committee on Banking, Trade and Commerce in 2007.

Note 7: The United States Bankruptcy Court for the District of Delaware in In Re: Mid-American Waste Systems, Inc., 228 B.R. 816 (Bankr. Del. 1999) indicated that this provision

applies to underwriters' claims, and reflects the policy rationale that such stakeholders are in a better position to evaluate the risks associated with the issuance of stock than are general creditors.

TAB 17

COURT FILE NO.: 32-OR-00137986
32-OR-00138325
DATE: 20031124

ONTARIO

SUPERIOR COURT OF JUSTICE

BANKRUPTCY OF TELEMARK INC. AND TELEMARK INTERNATIONAL INC.	)	
	)	**MOTION HEARD:** November 17, 2003
	)	**ORAL REASONS DELIVERED:**
	)	November 18, 2003

GROUND J.

ORAL REASONS

[1] The motion for declaratory orders declaring that the claims of the moving parties in the bankruptcies of Telemark Inc. and Telemark International Inc. are valid and subsisting claims was issued July 22, 2003 being within 30 days of the date of the Notices of Disallowance. Accordingly, I do not think that Subsection 135(4) of the *Bankruptcy and Insolvency Act* is a bar to the motion before this court. I also do not think that framing the proceeding as a motion for declaratory relief rather than as an appeal from the disallowance by the Trustee is fatal or renders the proceeding anullity. The situation is not, in my view, analogous to the situations in *Clarke Road Building Suppliers* where there was nothing before the court constituting a notice of motion or the situation in *Re Taylor Ventures Ltd.* where there appears to have been nothing before the court setting out the relief requested.

[2] There is clearly jurisdiction under subsection 192(2) of the *Bankruptcy and Insolvency Act* for a judge to hear and determine appeals from the decision of a trustee allowing or disallowing a claim and the bringing of the proceeding by way of a motion for declaratory relief rather than by way of an appeal is at most an irregularity which can be excused. Certainly the Trustee was in no way misled as to the purpose of the proceeding or the relief sought.

[3] On the merits of the appeal, the Notices of Disallowance are all identical and do not distinguish between the claims in the estate of Telemark Inc. and the claims in the estate of Telemark International Inc.

[4] There are four stated reasons for the disallowance as follows:

1. The proof of claim is not on behalf of a creditor of the Bankrupt.
2. The proof of claim fails to refer to a statement of account showing the particulars of the claim or other evidence by which it can be substantiated and thus fails to comply with section 124(4) of the Act. There is no proof that there is any money owing.
3. The proof of claim has attached to it a statement of claim in a class action which is yet to be certified; the statement of claim is not evidence and, in any event, it sets out no specific amount as owing to the alleged creditor.
4. The other attachment to the proof of claim is the order of the Honourable Madam Justice Aitken. This order addresses to some extent the claim set out in the statement of claim. However, this order is not evidence in support of the claim. Counsel for the alleged creditor has advised in writing that the order is "not a claim provable in bankruptcy" and the Trustee agrees with him in this regard. The matters raised in the order are not something provable in bankruptcy.

[5] The first reason, that the proof of claim is not on behalf of a creditor, seems to me to beg the question. Whether or not the person submitting the claim is a creditor will depend upon the outcome of the litigation as it proceeds.

[6] As to the second reason, that there is no statement of account showing particulars of the claim, the nature of the claims made by the moving parties are not such that statements of account would be generated but, in any event, the claims in the estate of Telemark Inc. do set out specific particulars and specific dollar amounts.

[7] The third and fourth reasons for the disallowance appear to relate to the claims in the estate of Telemark Inc. and seem to be based on the statement of claim and the order of Justice Aitken attached to the statement of claim not being evidence of the amount of $350,000 claimed by the moving parties or of any other specific amount.

[8] It is acknowledged by the moving parties that these claims against Telemark Inc. are an estimate of what their damages would be in an action against Telemark Inc. and are based on an estimate of franchise fees paid and losses incurred as a result of the alleged improper activities of Telemark Inc. These claims are clearly contingent and for unliquidated amounts but, under the provisions of Sections 121 and 122 of the *Bankruptcy and Insolvency Act*, that is no bar to the claims being allowed.

[9] The criteria which the court must apply in determining whether such claims are provable is that they must be claims which could be recoverable by legal process and they must not be too remote or speculative. The nature of these claims are such that the moving parties could be awarded damages if they are successful in the pending litigation and, in my view, they are not too speculative or remote as evidenced by the findings of Justice Aitken that t he moving parties have a good *prima facie* case for breach of contract and bad faith on the part of Telemark Inc.

[10] Accordingly, an order will issue that the proofs of claim of the moving parties in the bankruptcies of Telemark Inc. and Telemark International Inc. shall be allowed by the Trustee and valued and, if the Trustee is unable to value the claims, the matter shall be referred to this court for determination upon such evidence as may be adduced by the parties in respect of such valuation.

[11] Counsel are directed to make brief written submissions to me on the costs of this proceeding on or before December 19, 2003.

_____

Ground J.

Released: November 24, 2003

COURT FILE NO.: 32-OR-00137986
32-OR-00138325
DATE: 20031124

ONTARIO

SUPERIOR COURT OF JUSTICE

BANKRUPTCY OF TELEMARK INC. AND TELEMARK INTERNATIONAL INC.

ORAL REASONS

Ground J.

Released: November 24, 2003

TAB 18

IN THE SUPREME COURT OF BRITISH COLUMBIA

Citation: *Tudor Sales Ltd. (Re),* 2017 BCSC 119

Date: 20170125
Docket: B131477
Registry: Vancouver

Between:

IN THE MATTER OF THE BANKRUPTCY OF TUDOR SALES LTD.

Before: The Honourable Mr. Justice A. Saunders

Reasons for Judgment

Counsel for the Trustee, Boale, Wood & Company Ltd:	S. H. Stephens
Counsel for the Applicant Cascade Steel Rolling Mills Inc.:	W. B. Milman K. Macdonald
Counsel for the Applicant Tavi Eggertson:	D. K. Magnus
Place and Date of Hearing:	Vancouver, B.C. January 8, 2016
Further Written Submissions of Cascade Steel Rolling Mills Inc.:	April 19; June 2, 2016
Further Written Submissions of Tavi Eggertson:	May 19, 2016
Place and Date of Judgment:	Vancouver, B.C. January 25, 2017

Introduction

[1] The applicant Cascade Steel Rolling Mills Inc. ("Cascade"), an acknowledged unsecured creditor of the bankrupt, Tudor Sales Ltd. ("Tudor"), seeks an order under s. 135(5) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985 c. B-3 [*BIA*], that the proof of claim and proof of security of Tavi Eggertson ("Mr. Eggertson") be expunged, reduced, or subordinated to the claims of other creditors.

[2] The applicant Mr. Eggertson, who claims to be a secured creditor, seeks an order that all funds currently held in trust by the trustee, Boale, Wood & Company Ltd. ("Boale, Wood"), be released to him.

[3] The applications were argued on January 8, 2016. Cascade and Tudor were subsequently given leave to make further written submissions as to the import of the decision of the Ontario Superior Court of Justice in *U.S. Steel Canada Inc. (Re)*, 2016 ONSC 569 [*U.S. Steel*]. Those submissions were received by June 2, 2016. A further written submission filed by counsel for Mr. Eggertson, purportedly as sur-reply, has been disregarded, as it was, in its entirety, not proper sur-reply but essentially repetition of arguments previously advanced.

Background

[4] Tudor made an assignment in bankruptcy on November 20, 2013. At that time, Tudor's most recent (unaudited) financial statements were for the fiscal year ending October 31, 2012. Those financial statements recorded shareholder loans owed to Mr. Eggertson, who was a shareholder of Tudor, and its sole officer and director, in the amount of $1,361,359. This loan liability as recorded in the financial statements arose out of two purported loans made to Tudor by Mr. Eggertson in 2005 and 2006 (collectively, the "2005-06 Advances").

[5] Tudor's Form 78 Statement of Affairs, sworn to by Mr. Eggertson on November 20, 2013, included Mr. Eggertson amongst the listed secured creditors. It asserted that Mr. Eggertson's secured claim was in the amount of $1,770,656.70. How that claim amount was arrived at is not disclosed. Mr. Eggertson's evidence

when examined on November 26, 2014 is that this amount was “a guess at best”. As will be seen, since then Mr. Eggertson has at least implicitly resiled from that claim amount.

[6] Cascade, a trade creditor of Tudor, is the single largest unsecured creditor. Its claim of $1,367,746.25 represents approximately 28% of the bankrupt’s total unsecured debt. That claim amount is not in dispute.

[7] Acting under a general security agreement dated March 1, 2006 and registered November 18, 2011 (the “GSA”), Mr. Eggertson sought the appointment of Boale, Wood as receiver. After satisfying itself of the validity of Mr. Eggertson’s security, by way of obtaining an independent legal opinion, Boale, Wood accepted the appointment in November 2013.

[8] Boale, Wood prepared and distributed a trustee’s preliminary report to creditors, in December 2013. That preliminary report stated that there would be a significant shortfall to the secured creditors, and there would be no funds available for distribution to the unsecured creditors, among which was Cascade.

[9] After payment of other secured claims, Boale, Wood – presumably, acting on the belief that the indebtedness to Mr. Eggertson was secured by his GSA – paid out $500,000 to Mr. Eggertson, in March 2014. That left approximately $600,000 on hand for distribution.

[10] Following the aforesaid $500,000 distribution to Mr. Eggertson, Cascade advised Boale, Wood that it was investigating the validity of, and/or the amount secured by, Mr. Eggertson’s GSA. Boale, Wood determined that no further distributions would be made until the issues related to Mr. Eggertson’s security were resolved.

[11] In May 2014, Cascade requested that Boale, Wood undertake an examination of Mr. Eggertson; Boale, Wood declined to do so, citing a lack of funds.

[12] Cascade then applied for an order under s. 163(2) of the *BIA* that Mr. Eggertson undergo an examination under oath. That order was granted by Mr. Justice Leask, on August 21, 2014.

[13] In response to that application, Mr. Eggertson filed an affidavit in which he asserted that his secured claims were comprised not only of the approximately $1.37 million in shareholder loans described in Tudor's financial statements, but also a further $1.92 million in loans he had made to Tudor in 2011 and 2012 (the "2011-12 Advances"). He put his total claim, net of the $500,000 received in March 2014, at $2,781,359. He affirmed that claim in a formal Proof of Claim delivered on October 31, 2014, in response to a Notice by Trustee Requiring Filing of Proof of Security.

[14] Cascade examined Mr. Eggertson under oath on November 26, 2014.

[15] In the course of Boale, Wood's review of Mr. Eggertson's claim, the trustee identified documentation – in evidence on these applications – that the 2011-12 Advances had been recorded in Tudor's books as being due from "TE Steel", a related company whose expenses Tudor had funded. Mr. Eggertson was advised of Boale, Wood's position that those advances should not form part of his claim against Tudor, by way of an email from the trustee's legal counsel dated December 9, 2014. The materials filed on these applications do not disclose any response to this position having been made by Mr. Eggertson.

[16] On the basis of the transcript of the examination of Mr. Eggertson, Cascade sought a ruling from Boale, Wood in January 2015, asking that Mr. Eggertson's proof of security be disallowed under s. 135 of the *BIA*, and that the trustee demand the return of the previously distributed funds. Boale, Wood declined to do so, again citing a lack of resources, leaving it to the creditors to bring the present applications.

Positions of the Parties

[17] Mr. Eggertson's evidence is that the 2005-06 Advances consisted of two loan amounts made by him: $890,000 on October 29, 2005; and a further $500,000 in

December 2006. He says that there were subsequently adjustments in Tudor's accounts as a result of payments made to him by Tudor, resulting in a net reduction of $28,641, leaving a total shareholder loan of $1,361,359.

[18] The first payment of $890,000 was money that his accountants (also Tudor's accountants) had recommended be paid to him by the company as a bonus, in addition to his salary. He took the bonus, in the sense that he declared it as income on his tax return, but says that he left the money in the company as a loan.

[19] Determination of the amount of that bonus had been, as he described it, tax-driven. His evidence is that "everything that I did when I worked at Tudor Sales was tax driven".

[20] The $890,000 payment was originally described in Tudor's October 31, 2005 financial statements as "unsecured, non-interest bearing and … no fixed terms of repayment". Mr. Eggertson contends that it was always intended that this money be repaid to him eventually.

[21] The $500,000 loan of December 2006 was made by him to Tudor, he says, because the money was "needed for growth". Elsewhere in his evidence, he stated that the money was needed by the company "to buy product".

[22] After the GSA was executed in March 2006, notes in subsequent financial statements described his shareholder loans – both the $890,000 bonus left in the company, and the $500,000 loan he made in December 2006 – as interest-bearing. However, the notes continued to refer to the loans as "unsecured". Although Mr. Eggerston signed off on the financial statements each year, he says these notes were incorrect, in that he intended the GSA to cover those loans. The financial statements began to refer to the shareholder loans as secured, beginning in 2011.

[23] There was no written documentation of those shareholder loans, no fixed interest rate, or formula by which the interest rate could be determined, and no schedule for repayment. The loans are described in the October 31, 2012 financial statements of Tudor under a note that reads:

> Advances, secured by a general security agreement over all present and future personal property, bears interest of 8% (October 31, 2011 – 8%; November 1, 2010 – 36%) per annum with no fixed terms of repayment.

[24] Mr. Eggertson's evidence is that the interest rate at which he was paid each year in respect of his shareholder loans fluctuated with the fortunes of the company, depending on advice received from his accountants. At times, when the company was doing well, the interest rate was as high as 36%. At other times – in particular, for the fiscal year 2009 – the interest rate set by the accountants would turn out to have been too high relative to the company's performance, and the financial statements would record him as having partially forgiven interest payment.

[25] Mr. Eggertson says that the 2011-12 Advances were made on the expectation that they were loans to Tudor secured by the GSA. These advances were used to fund the operations of T. E. Sales Inc. (formerly T. E. Steel Sales Inc.), a company controlled by his wife. (He says that the financial statements of Tudor are mistaken in referring to T. E. Sales as a related company.) T. E. Sales Inc. had no assets; it, in turn, had used the advances to fund a tequila importation venture in which Mr. Eggertson had an interest.

[26] The documentation relied upon by Boale, Wood in December 2014, in denying Mr. Eggertson's claim for these advances, is a Detailed Trial Balance. It records certain expenditures reallocated by the accountants, including an amount respecting "Casi di Tavi", which I infer is the company Casa de Tavi, identified by Mr. Eggertson as one of the entities involved in the tequila venture in which he had an ownership interest. There are other references to "bottles" and "liquor", and numerous references to "TT" and "TE Steel TT", which I infer, from his description of the venture in his examination evidence, to be related to "Tavi Tequila".

[27] Mr. Eggertson's evidence is that though the tequila venture was in its infancy, he hoped to build the brand, and hoped that Tudor would eventually be repaid out of profits from the sale of "Tavi Tequila" imported into British Columbia. He regarded this, he says, as an investment by Tudor. Elsewhere in his evidence, he says that he

intended to make a gift to Tudor of all rights to Tavi Tequila, once the venture began consistently generating revenue.

[28] Mr. Eggertson's position is that the Tudor financial statements are inaccurate and incomplete, in that they do not include the 2011-12 Advances used to fund those expenditures in the shareholder loans. He says that he had an ongoing disagreement with his accountants as to the allocation of expenses amongst Tudor and his other ventures. That disagreement led to him firing his accountants, he says, after the 2012 financial statements were prepared.

[29] Mr. Eggertson's position is that whether his full claim is recognized, or whether he is obliged to discount the amount of the 2011-12 Advances and limit his claim to the remaining balance of the 2005-06 Advances, his secured claims exceed the amount remaining in trust with Boale, Wood, and he says he is entitled to payment of that amount in full.

[30] Cascade's primary submission is that the 2005-06 Advances, though carried on the books of Tudor as loans, are properly characterized as equity, and must be subordinated to the claims of Tudor's creditors.

[31] Alternatively, Cascade asserts that if the 2005-2006 Advances were loans, those loans were repaid in full through Mr. Eggertson having been paid an exorbitant salary, and through him having been paid interest at exorbitant rates, as high as 36%.

[32] With respect to the 2011-12 Advances, Cascade says that Tudor's 2012 financial statements report advances made to "related parties" that were not in fact related to Tudor but were in fact ventures owned or controlled by Mr. Eggertson, or from which he stood to profit personally, and that Mr. Eggertson simply used Tudor as a vehicle to make those expense payments. Cascade submits, essentially, that Mr. Eggertson's use of Tudor as a vehicle was a matter of convenience to him and that he cannot shelter his payments made through Tudor under Tudor's GSA, thereby defeating the legitimate commercial interests of Tudor's trade creditors.

[33] Cascade relies upon ss. 137, 139, and 140.1 of the *BIA*, which provide as follows:

> **Postponement of claims — creditor not at arm's length**
>
> 137 (1) A creditor who, at any time before the bankruptcy of a debtor, entered into a transaction with the debtor and who was not at arm's length with the debtor at that time is not entitled to claim a dividend in respect of a claim arising out of that transaction until all claims of the other creditors have been satisfied, unless the transaction was in the opinion of the trustee or of the court a proper transaction.
>
> …
>
> **Postponement of claims of silent partners**
>
> 139 Where a lender advances money to a borrower engaged or about to engage in trade or business under a contract with the borrower that the lender shall receive a rate of interest varying with the profits or shall receive a share of the profits arising from carrying on the trade or business, and the borrower subsequently becomes bankrupt, the lender of the money is not entitled to recover anything in respect of the loan until the claims of all other creditors of the borrower have been satisfied.
>
> …
>
> **Postponement of equity claims**
>
> 140.1 A creditor is not entitled to a dividend in respect of an equity claim until all claims that are not equity claims have been satisfied.

Discussion and Analysis

[34] With respect to the shareholder loans claim arising out of the 2005-06 Advances, the threshold question is whether the amounts advanced to Tudor by Mr. Eggertson are properly characterized as a debt, or as equity.

[35] These purported loans having been a non-arm's-length transaction, I am guided by the description of the court's role in characterizing, or re-characterizing, such payments, as recently set out by Justice Wilton-Siegel in *U.S. Steel:*

> [167] Where … the parties are not at arm's length, the issue is not what the parties say they intended regarding the substance of the transaction as a matter of contractual interpretation. The expressed intention of the parties is clear. However, given the absence of any arm's length relationship, there can be no certainty that the language of the agreements reflects the underlying substantive reality of the transaction. Accordingly, the issue for a court is whether, as actually implemented, the substance of the transaction is, in fact, different from what the parties expressed it be in the transaction documentation.

> [168] In other words, the task of a court is to determine whether the transaction in substance constituted a contribution to capital notwithstanding the expressed intentions of the parties that the transaction be treated as a loan. It is therefore not appropriate to limit the inquiry into the intentions of the parties to a review of the form of the transaction documentation. Such an exercise reduces to a "rubber stamping" of the determination of a single party to the transaction, i.e., the sole shareholder, and it does not address the substance of the transaction as it was actually implemented. In such circumstances, the determination of whether a particular claim is to be treated as debt or equity must address not just the expressed intentions of the parties as reflected in the transaction documentation but also the manner in which the transaction was implemented and the economic reality of the surrounding circumstances.

[36] Further on in that judgment, Wilton-Siegel J. discussed the various factors which he found appropriate to determination of the debt claim before him, given the particular financial instruments utilized by the parties. He began that discussion with an explanation of the difference between equity and debt from an expert report tendered by one of the parties, authored by an economist, Dr. John Finnerty, which I also adopt:

> [183] An appropriate starting point is the definition of debt and equity for financial purposes set out in paragraphs 32 and 34 of the Finnerty Report:
>
> > At its heart, the difference between equity and debt lies in the fundamental nature of their respective claims on the assets and cash flow of the company. Debt involves borrowing funds subject to a legal commitment to repay the borrowed money with interest at an agreed rate by a stated maturity date. This commitment is embodied in a contract, and this contract is implemented by the borrower. Lenders receive a contractually agreed set of cash flows, typically through periodic interest payments and one or more principal repayments, the last of which occur on the maturity date. … In contrast to debt, an equity claim entitles the holder to a share of the company's profits and residual cash flows after the company has made all the contractually required debt service payments. That is, the debt ranks senior to the equity with respect to the company's cash flows. Similarly, the debt ranks senior to the equity in the event the company must be liquidated and its assets sold to repay its debt obligations. The equityholders get what is left after the holders of the debt have been paid in full; if the debtholders can't get paid in full, then the equityholders get nothing.

[37] The characterization of the 2005-06 Advances as equity, and not debt, is most strongly supported by the variable nature of the interest payments recorded in the financial statements as having been made to Mr. Eggertson. As a consequence of being variable with the company's profitability, the amount of the payments made

to Mr. Eggertson could not have been determined each year until any and all current liabilities to secured and unsecured creditors had been satisfied. As noted above in the quotation from the Finnerty Report in *U.S. Steel*, “debt ranks senior to the equity with respect to the company’s cash flows”. Functionally, therefore, Tudor’s payments to Mr. Eggertson were being treated as subordinated to all such current liabilities, a fact which is inconsistent with his claim to secured creditor status.

[38] Furthermore, the nature of the company’s liability to Mr. Eggertson was more consistent with equity than with debt, in that there was no schedule for repayment of these advances, and there was no certain formula to determine the interest amount. Payments, rather, were discretionary, based on the advice of the accountants, and varying with Tudor’s profitability. The ability to draw payment in this manner is not normally incidental to the rights of a creditor; instead, it is a hallmark of ownership.

[39] It is not the lack of a strict schedule for repayment in itself that is relevant; neither do I give any weight to the absence of loan documentation. This is because the relationship of a wholly-owned subsidiary to its parent obviates the need for same: see *U.S. Steel* at para. 217. It is, instead, the nature of those interest payments that reveals the true substance of the transaction.

[40] This characteristic of the transaction – the variable nature of the interest payments, fluctuating with the company’s profitability – is, I find, sufficient in itself to lead to the 2005-06 Advances being characterized as equity. In addition, I also regard the circumstances surrounding the 2005-06 Advances as germane. At the time of the first of those advances, October 29, 2005, Mr. Eggertson was not a shareholder of Tudor; the company’s sole shareholder was his father, Donald Eggertson. However, as disclosed in the company’s securities register, Mr. Eggertson became a shareholder as of January 1, 2006, only approximately two months later, when his father transferred nine of his 100 Class A common shares to Mr. Eggertson. There is no record of any consideration for the transfer having been paid. There is no evidence that it was a gift.

[41] In December 2006, Mr. Eggertson made his second advance, of $500,000. The security register discloses that that same month, his nine Class A common shares – a 9% holding – were exchanged for 100 Class D redeemable preferred shares. Tudor's 2007 financial statements indicate those shares were redeemable for $2,542,539. They therefore represented either approximately 50% or 67% of the value of the company (depending if the value of his father's remaining Class D shares was $1,231,538 – the redemption value noted in the 2007 financial statements – or $2.5 million, the figure at which Mr. Eggertson deposed those shares to have been redeemed in 2010).

[42] I agree with Cascade's submission that the very close proximity in time between these advances made by Mr. Eggertson, and at first his acquisition of a shareholder interest, and then the increase in value of that interest, strongly implies that his advances were in substance consideration paid for his ownership stake, making them equity contributions.

[43] The existence of the GSA does not assist Mr. Eggertson. The GSA itself makes no specific reference to the 2005-06 Advances. In fact, the shareholder loans arising out of those advances were not even described as secured loans in Tudor's financial statements until 2011, when the company went into default on its lending covenants, reinforcing the view that the advances were not originally intended as secured debt. In any event, as *U.S. Steel* makes clear, what is at issue is not the superficial appearance of the transaction or transactions arising out of the transaction documentation, but the manner in which the transaction or transactions were actually implemented in the circumstances of the surrounding economic reality.

[44] I therefore find Mr. Eggertson's claim in respect of the purported shareholder loans of $1,361,359 to be in respect of an equity claim, and subordinated to all creditor claims, pursuant to s.140.1 of the *BIA*.

[45] Alternatively, if characterized more appropriately as debt, rather than equity, Mr. Eggertson's claim would fail by reason of s.139 of the *BIA*. That section is premised on there being a contract between lender and company under which the

loan is to be repaid out of a share of profits, or is to receive a rate of interest varying with the profits. The evidence clearly discloses that such interest was paid by Tudor to Mr. Eggertson. The loans being non-arm's-length transactions, the intention of Mr. Eggertson to have Tudor pay him interest varying with the profits is sufficient to bring the loans within the ambit of s.139. Although no formal written contract existed between these two non-arm's length parties, Mr. Eggertson cannot thereby claim to be in a stronger position as a consequence.

[46] Nor do I find Mr. Eggertson has any legitimate claim arising out of the 2011-12 Advances. Mr. Eggertson presents no accounting evidence supporting his position that the tequila business expenses ought properly to have been allocated to Tudor. Nor is there any evidence that Tudor was regarded as being indebted to him for those advances, or that the flow of monies through Tudor's accounts to T. E. Steel and then to the tequila venture represented a *bona fide* investment on behalf of Tudor. Tudor was not a shareholder in Casa de Tavi; Mr. Eggertson was. It was his venture, regardless of whether he had a genuine intention that it might one day benefit Tudor.

[47] Under s.137(1) of the *BIA*, a non-arm's-length transaction may only support a claim to a dividend in respect of a bankruptcy claim arising out of that transaction, in preference to other creditors' claims, when the transaction is judged to be "proper". I am not satisfied that Mr. Eggertson's investment in his tequila venture is properly regarded as an indirect investment achieved by means of a loan to Tudor. There is simply no justification for allowing Mr. Eggertson the luxury of securing his investment in the venture through the mechanism of the GSA granted by Tudor, and thereby defeat the legitimate interests of trade creditors.

[48] In my view, Cascade is correct in arguing that Mr. Eggertson, as a non-arm's length party, bears the onus of proving the transactions are "proper". But if I am wrong in that view, I do nevertheless regard it as proven on the evidence that the 2011-12 Advances were not proper debt transactions as between Mr. Eggertson and Tudor.

[49] For these reasons, the application of Mr. Eggertson is dismissed, and the application of Cascade is allowed.

"A. Saunders J."

TAB 19

CITATION: U.S. Steel Canada Inc. (Re), 2016 ONSC 569
COURT FILE NO.: CV-14-10695-00CL
DATE: 20160229

SUPERIOR COURT OF JUSTICE - ONTARIO

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

AND IN THE MATTER OF A PROPOSED PLAN OF COMPROMISE OR ARRANGEMENT WITH RESPECT TO U.S. STEEL CANADA INC.

BEFORE: Mr. Justice H. Wilton-Siegel

COUNSEL: *Michael E. Barrack, Robert Thornton, Jeff Galway, Kiran Patel* and *Max Shapiro,* for United States Steel Corporation

Alan Mark, Peter Ruby, Tamryn Jacobson, Logan Willis and *Jesse-Ross Cohen,* for the Province of Ontario

Gordon Capern, Kris Borg-Olivier and Denise Cooney for USW and Locals 1005 and 8782

Andrew Hatnay, Barbara Walancik and *Adrian Scotchmer,* Representative Counsel for the non-unionized active employees and retirees

Sharon Kour, for the Applicant U.S. Steel Canada Inc.

Robert Staley, Jonathan Bell and William Bortolin, for the Monitor Ernst & Young Inc.

HEARD: January 14, 15, 20, 21, 22, 25, 26 and 27, 2016

ENDORSEMENT

[1] In this proceeding, United States Steel Corporation ("USS") seeks a determination of 14 Proofs of Claim (the "USS Claims") filed in these proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "CCAA") regarding U.S. Steel Canada Inc. ("USSC").

[2] Objections to the treatment of certain of these Claims as debt rather than as "equity claims" for the purposes of the CCAA, and to the enforceability of the security asserted in respect of certain of these Claims, have been filed by each of: (1) the United Steel, Paper and Forestry, Rubber, Manufacturing, Energy, Allied Industrial and Service Workers International Union (the "USW") on its own behalf and on behalf of USW Local 1005 and USW Local 8782 (collectively, the "Union"); (2) Her Majesty the Queen in Right of Ontario and the Superintendent of Financial Services (Ontario) in his capacity as administrator of the Pension

Benefits Guarantee Fund (collectively, the "Province"); and (3) Representative Counsel to all non-USW active employees and retirees of USSC (collectively, the "Objecting Parties").

[3] This motion principally addresses the objections filed by the Objecting Parties (the "Objections"). The following are the USS Claims in respect of which Objections have been made:

Claim Reference #	Description of Claim	Amount of Claim
9	Unsecured Term Loan	$1,847,169,934
10	Unsecured Revolver Loan	U.S. $120,150,928
11	Secured Revolver Loan	U.S. $72,938,390
11(a)	Secured Cliffs LRD Transaction	U.S. $14,538,463
11(b)	Secured Credit Support Payments	U.S. $3,742,479
11(c)	Secured Intercompany Trade	U.S. $31,252,193

The Claim numbers above, and amounts reflected in this table, are taken from the Third Supplementary Seventh Report of the Monitor dated July 29, 2015 (the "Third Supplementary Monitor's Report") at para. 11.

[4] In these Reasons, Claims #9 and #10 are referred to as the "USS Unsecured Claims" and Claims #9, #10 and #11 are referred to collectively as the "USS Debt Claims". In addition, Claims #11, #11(a), #11(b) and #11(c) are referred to as the "USS Secured Claims", and Claims #11(a), #11(b) and #11(c) are referred to as the "USS Remaining Secured Claims".

Background

[5] The following is a brief summary of the background to this proceeding. Further detail regarding the relationship between USS and USSC and the USS Claims that have given rise to the Objections is set out below.

USSC

[6] USSC is an integrated steel manufacturer that conducts most of its business from two large steel plants located in Ontario: the Hamilton Works located in Hamilton, Ontario and the Lake Erie Works located in Nanticoke, Ontario.

[7] USSC is an indirect wholly-owned subsidiary of USS. Prior to its acquisition by USS in 2007, USSC was known as Stelco Inc. ("Stelco").

[8] As a result of its financial difficulties, USSC applied for relief under the CCAA and was granted CCAA protection pursuant to an Initial Order dated September 16, 2014 (the "Filing Date") (as amended and restated from time to time, the "Initial Order").

The USS Parties

[9] USS is an integrated steel producer with major operations in North America and Central Europe. USS is a publicly-traded, Delaware corporation and its shares are listed for trading on the New York Stock Exchange.

[10] 1344973 Alberta ULC ("ABULC") was an Alberta corporation incorporated on August 22, 2007 to be the acquisition vehicle for the purposes of the USS acquisition of Stelco.

[11] U.S. Steel Canada Limited Partnership ("Canada LP") is a limited partnership formed under the laws of Alberta. Canada LP is an indirect wholly-owned subsidiary of USS. At the time of the USS acquisition of Stelco, Canada LP owned all the outstanding shares of ABULC and was, therefore, ABULC's direct parent. As a result of the amalgamation of ABULC and USSC on December 31, 2007 described below, Canada LP has become the direct parent of USSC.

[12] United States Steel Credit Corporation ("Credit Corp") was a Delaware corporation that was a wholly-owned subsidiary of USS. Credit Corp was merged into another wholly-owned subsidiary of USS on December 20, 2013.

[13] U.S. Steel Kosice s.r.o. ("USS Kosice") is a Slovakian corporation that is an indirect wholly-owned subsidiary of USS.

The USS Acquisition of Stelco Inc. in 2007

[14] On August 26, 2007, the USS board of directors approved the USS acquisition of Stelco, and USS, Stelco and ABULC entered into an arrangement agreement giving effect to the proposed transaction. The plan of arrangement by which the acquisition was implemented was subsequently approved by the Ontario Superior Court of Justice on October 30, 2007, and the acquisition transaction closed on October 31, 2007 (the "Acquisition").

Financing the Acquisition and the Flow of Funds

[15] The total amount spent by USS in connection with the Stelco acquisition was approximately $1.939 billion, or U.S. $2.056 billion at then prevailing exchange rates. The relevant corporate structure and the flow of funds are shown on the Funds Flow Chart attached as Schedule A to these Reasons. In these Reasons, all dollar amounts are denominated in Canadian dollars unless otherwise specifically indicated.

[16] ABULC was the acquisition vehicle that directly acquired Stelco. ABULC was financed by the following loans and capital contributions:

(a) Canada LP loaned ABULC $700 million pursuant to a loan agreement dated October 29, 2007 described below (the "Term Loan");

(b) Canada LP provided ABULC with equity in the amount of $600 million; and

(c) Credit Corp loaned ABULC approximately U.S. $744 million pursuant to a loan agreement dated October 29, 2007 described below (the "Credit Corp Loan").

[17] ABULC used the funds received from Canada LP and Credit Corp as follows: (1) ABULC used $1.046 billion to purchase the outstanding shares of Stelco; (2) ABULC loaned Stelco approximately $741 million, which Stelco used to pay out its third party debt (other than a loan from the Province of Ontario); (3) ABULC loaned Stelco approximately $59 million, which Stelco used to pay out its option holders; (4) ABULC loaned Stelco approximately $61 million, which Stelco used to pay out its warrant holders; (5) ABULC loaned Stelco $32.5 million, which Stelco used to make a payment to its four main pension plans; and (6) ABULC loaned Stelco $40 million to fund Stelco's working capital.

[18] The funds used to acquire Stelco were derived from multiple sources. First, USS obtained new debt financing in the principal amount of U.S. $900 million in the form of facilities provided by a banking syndicate led by J.P. Morgan Chase Bank, N.A. These facilities comprised an unsecured three-year term loan in the principal amount of U.S. $500 million and an unsecured one-year term loan in the amount of U.S. $400 million. The one-year term loan was subsequently refinanced by USS as part of a larger offering of ten-year bonds in the public market. Second, USS obtained approximately U.S. $400 million by drawing on an existing receivables purchase facility. Third, USS utilized approximately U.S. $153 million of cash on hand at the USS level and €434,415,519.56, or $597,860,287.50, of cash on hand in USS Kosice.

[19] The source of the financing for the Acquisition, the structure of the Acquisition and the flow of funds to ABULC for such purposes was developed by USS between the date of the Arrangement Agreement and the date of the Acquisition. The principal consideration in the development of this structure was tax-efficiency from the perspective of USS. With respect to ABULC, the amounts received by it as debt and equity were driven by the "thin capitalization" rules under the *Income Tax Act*, R.S.C. 1985, c. 1 (5th Supp.). In addition, the amount of the funding reflected a USS policy of avoiding any secured third party indebtedness at the level of any subsidiary. As a result, it was necessary to fund Stelco with the amount necessary to repay all outstanding third party debt at the date of the Acquisition, other than a loan from the Province.

Post-Acquisition Corporate Reorganization & Refinancing

[20] On November 1, 2007, immediately following the Acquisition, Stelco was renamed U.S. Steel Canada Inc.

[21] Between October 31, 2007 and the year-end, the Credit Corp Loan was repaid in full. Certain of the repayments were made from additional advances under the Term Loan which are described in greater detail below.

[22] Following such additional advances by Canada LP to ABULC under the Term Loan in 2007, the outstanding principal amount outstanding under the Term Loan on December 31, 2007 was $1,227,363,149.82. The total amount outstanding on that date including accrued interest was $1,240,009,143.

[23] ABULC and USSC amalgamated on December 31, 2007 to continue as USSC (the "Amalgamation"). As a result of the Amalgamation, the obligations of ABULC under the Term Loan became obligations of the amalgamated entity, USSC.

The History of the Credit Corp Loan

[24] As described above, pursuant to the Credit Corp Loan, Credit Corp advanced U.S. $744,463,605 to ABULC on or about October 31, 2007. The funds provided by the Credit Corp Loan were notionally intended to fund Stelco's third party debt at the date of acquisition that was denominated in U.S. dollars. USS intended the facility to be a short-term facility that would be repaid within two months. Larry Brockway, the Senior Vice-President, Chief Financial Officer and Chief Risk Officer of USS ("Brockway"), testified that the "purpose of the agreement was to help stair-step the structure into a more permanent structure as part of the ultimate steps between the acquisition and year end".

[25] Consistent with this objective, the Credit Corp Loan was repaid by means of: (1) a repayment of approximately U.S. $26 million in November 2007; (2) a repayment of approximately U.S. $41 million on December 4, 2007, which was funded by an advance to ABULC under the Term Loan on the same day described below; (3) a U.S. $87 million repayment by ABULC on December 21, 2007, comprised of U.S. $10 million presumably funded out of a U.S. $20 million equity injection from Credit Corp to ABULC on the same day and application of U.S. $77 million out of the $470 Million Advance described below; and (4) a reduction in the amount of approximately U.S. $595 million pursuant to the SHC Transaction described below.

The SHC Transaction

[26] The following summarizes the description of the SHC Transaction set out in the Third Supplementary Monitor's Report.

[27] At the time of the Acquisition, Stelco indirectly owned all of the outstanding shares of Stelco Holding Company ("SHC"), a corporation incorporated under the laws of Delaware. SHC's principal assets were interests in two mining joint ventures – Hibbing Taconite Company ("Hibbing") and Tilden Mining Company ("Tilden").

[28] At the time of the Acquisition, SHC had a liability to Stelco in the amount of approximately U.S. $393 million. This amount principally represented the excess of the amount owing by Stelco to SHC for iron-ore pellets produced by Hibbing and Tilden and shipped to Stelco, representing SHC's *pro rata* share of such production, less the amount of annual cash calls on SHC in respect of Hibbing and Tilden, which were paid by Stelco on behalf of SHC. This liability was booked as an advance from SHC to Stelco, and had increased in each year prior to 2007. The liability also included legacy liabilities of Stelco to certain other subsidiaries of SHC that were dormant. Stelco had not repaid any amount on account of these advances, and had no intention of doing so prior to the Acquisition, due to the adverse tax consequences of dividending the amount of any such payment back to Canada.

[29] The Acquisition presented an issue of tax inefficiency for USS, referred to as a "tax sandwich", that would result if distributions from SHC (as dividends or interest) were made to USSC in Canada and, in turn, distributed to USS in the United States. To address this issue, USS caused ABULC, USSC and SHC to enter into certain transactions which were effected by book entries in the financial accounts of the relevant corporations pursuant to a payment direction

agreement dated December 21, 2007 (the "Payment Direction") (collectively, the "SHC Transaction").

[30] The SHC Transaction involved the following steps:

(1) ABULC loaned USSC the amount of U.S. $393 million out of the $470 Million Advance (defined below);

(2) USSC repaid the outstanding advance to SHC in the same amount;

(3) USSC sold its equity interest in SHC to USS for consideration in the form of a promissory note dated December 31, 2007 in the principal amount of U.S. $595 million payable to the wholly-owned subsidiary of USSC that owned the shares of SHC. The face amount of the promissory note of U.S. $595 million represented USS' estimation of the fair market value of SHC at the time of the sale; and

(4) The promissory note was distributed by such wholly-owned subsidiary to USSC on December 31, 2007 which, in turn, assigned the note to Credit Corp in reduction of the remaining principal amount outstanding under the Credit Corp Loan, which was slightly less than U.S. $593 million.

[31] The effect of the SHC Transaction was to transfer ownership of SHC from USSC to USS by way of satisfaction of the remaining amount outstanding under the Credit Corp Loan as of December 31, 2007.

The Term Loan

[32] The following summarizes the provisions of the Term Loan that are relevant for the issues in this proceeding and the history of draws and accrued interest under the Term Loan resulting in the USS claim in respect of the Term Loan.

The Relevant Provisions of the Term Loan

[33] The Term Loan is an unsecured loan facility having a term of 30 years repayable by USSC at any time without premium or penalty. The full amount of the outstanding principal is therefore due on October 31, 2037, to the extent it is not repaid before that date. USS says that it selected a 30-year term for the Term Loan because it viewed its investment in Stelco as a long-term one. The 30-year term was also the maximum term countenanced for U.S. tax purposes.

[34] Interest on the Term Loan accrued daily and compounded semi-annually at an interest rate of 9.03% per annum. USS obtained and relied upon advice from an independent, third-party consultant regarding an acceptable interest rate for a company with a similarly rated risk for 30-year debt. Interest is payable on the last business day of the year on the second anniversary after the year in which it accrues. As a result, interest under the Term Loan was payable from 24 to 36 months after the date it began to accrue.

[35] The Term Loan was denominated in Canadian dollars. The Term Loan originally allowed for a maximum borrowing of $1 billion. The maximum availability under the Term Loan was increased from $1 billion to $1.5 billion on December 21, 2007. As mentioned, the

amount of $700 million was initially advanced on October 31, 2007. The Term Loan provided that further advances could be obtained "with prior written notice … pursuant to a request for advance" set out in a form similar to a scheduled document to the Term Loan.

[36] The loan agreement contains certain representations and covenants of ABULC/USSC and events of default. The events of default include an event of default if the borrower is "unable to meet debts". Upon the occurrence of an event of default, the maturity date is accelerated and Canada LP has the right to demand repayment.

History of Advances and Repayments under the Term Loan

[37] As mentioned above, Canada LP advanced $700 million to ABULC on October 31, 2007 in connection with the Acquisition. This amount became a direct obligation of USSC after the Amalgamation. In addition, during the period from the Acquisition to the Amalgamation, ABULC recorded three additional advances. On December 4, 2007, ABULC recorded two advances totaling approximately U.S. $61 million, of which U.S. $41 million was applied to reduce the Credit Corp Loan and the balance was advanced to USSC for working capital purposes. On December 22, 2007, ABULC recorded an advance of U.S. $470 million under the Term Loan pursuant to the Payment Direction (the "$470 Million Advance"). The foregoing advances under the Term Loan are collectively referred to as the "initial advances".

[38] During 2008, USSC made interest payments to Canada LP under the Term Loan totalling approximately $113 million. Of this amount, $99,940,908 was paid in October and November 2008. Such payments were made in advance of their due date under the Term Loan Agreement, which provided that such interest was not payable until December 31, 2010. In addition, USSC made a principal repayment of $19 million in January 2008. The only additional funding provided to USSC by USS or any of its affiliates in 2008 was an equity injection of approximately $55 million in October 2008.

[39] In 2009, USSC received additional advances from Canada LP under the Term Loan totalling $211.2 million. These advances were made during the months of February, June, September, November and December 2009. No interest or principal was paid during 2009. In addition, as set out in the table above, USS provided equity injections totalling $61 million during 2009. These capital contributions were made in February, July and October 2009.

[40] There were no further advances under the Term Loan after 2009. At the end of 2010, USS decided to waive the remaining interest that was due under the Term Loan in respect of interest accrued during 2008. Since there had been substantial interest payments made in 2008, the accrued interest that was waived in December 2010 was only $10.5 million. USS says that, given USSC's other funding needs at the time, the interest payment could only have been made if USSC received additional funding. Further, due to taxation on interest payments, it did not make economic sense to fund USSC with additional debt or equity in order to enable USSC to repay interest on the Term Loan. USS says that this was the first time that USS considered waiving interest due under the Term Loan. In other words, it asserts that it did not have such expectation at the time that it entered into the Term Loan.

[41] USS continued the practice of waiving interest in each year after 2010. Accordingly, in each of the years 2010 to 2013, USS waived approximately one-half of the accrued and unpaid

interest due in that year. In total, USS has waived interest obligations of USSC totaling approximately $428 million and has accrued interest under the Term Loan in approximately the same amount.

[42] As of the Filing Date, the total amount outstanding under the Term Loan, including accrued interest, was $1,847,169,934.

The Revolver Loan

[43] Pursuant to an agreement dated May 11, 2010 between USSC and Credit Corp (as amended from time to time, the "Revolver Loan Agreement"), Credit Corp established a Revolver Loan to provide working capital to USSC to support its operating activities. The Revolver Loan Agreement was subsequently amended successively by an agreement dated July 31, 2012 (the "First Revolver Amendment"), an agreement dated January 28, 2013 (the "Second Revolver Amendment") and an agreement dated October 30, 2013 (the "Third Revolver Amendment") in the circumstances described below. In these Reasons, the loan outstanding under the Revolver Loan Agreement, as so amended from time to time, is herein referred to as the "Revolver Loan" and the Term Loan and the Revolver Loan are collectively referred to as the "Loans" and individually are referred to as a "Loan".

[44] USS has filed two proofs of claim in respected of the Revolver Loan. The first claim is an unsecured claim (being Claim #10) in the amount of U.S. $120,150,928, representing the outstanding loan on October 30, 2013, together with accrued interest since that date. The second claim is a secured claim (being Claim #11) in the amount of U.S. $72,938,390, representing the loan advances since October 30, 2013 plus accrued interest. The following sets out the principal terms of the Revolver Loan, including the related security, and the history of advances and payments in respect of the Revolver Loan.

Terms of the Revolver Loan

[45] The Revolver Loan was originally an unsecured loan having a fifteen-year term. Accordingly, all outstanding advances are due on May 11, 2025. As mentioned, the Revolver Loan originally provided for a maximum availability of U.S. $350 million.

[46] Advances under the Revolver Loan accrued interest at the applicable federal interest rate for the month in which the advance was drawn and compounded interest semi-annually. The applicable interest rate as of the date of the Revolver Loan was 4.42% per annum.

[47] The loan agreement contains certain representations and covenants of USSC, including originally, a solvency representation, and events of default. The events of default include an event of default in the event that the borrower is "unable to meet debts". Upon the occurrence of an event of default, the maturity date is accelerated and Credit Corp had the right to demand repayment. The loan agreement is governed by the laws of the Commonwealth of Pennsylvania.

The History of Advances and Repayments Under the Revolver Loan

[48] Credit Corp advanced a total of U.S. $120 million under the Revolver Loan from its establishment in May 2010 through the third quarter of 2011. Of this amount, U.S. $75 million

was advanced in May 2010, U.S. $25 million was provided in two advances in August 2010, and a further U.S. $20 million was advanced in June 2011.

[49] In the period from November 2011 to April 2012, USSC had somewhat more stable cash flows. Credit Corp advanced approximately U.S. $136 million under the Revolver Loan during this period. During the same period, USSC made interest payments totaling almost U.S. $9 million and principal repayments of approximately U.S. $61.8 million under the Revolver Loan. Thereafter, the outstanding balance began to grow with additional advances in each month in 2012, other than October.

[50] By July 31, 2012, the outstanding principal balance of the Revolver Loan was, however, approaching the cap of U.S. $350 million. On that date, Credit Corp and USSC executed the First Revolver Amendment, which increased the maximum availability under the Revolver Loan to U.S. $500 million. Apart from removal of the solvency representation of USSC, the First Revolver Amendment did not otherwise amend the provisions of the Revolver Loan Agreement, including the events of default. The solvency representation of USSC was removed at the request of USSC's management, which had a concern about USSC's solvency given its recent losses and the level of its debt. The circumstances pertaining to this action are addressed further below.

[51] By January 28, 2013, however, after additional advances to USSC under the Revolver Loan, the outstanding principal balance of the Revolver Loan had again reached the maximum availability. USSC's business plan for 2013 indicated that it would need substantial additional financing during that year in order to finance its operations. Accordingly, on that date Credit Corp and USSC executed the Second Revolver Amendment, which increased the maximum availability under the Revolver Loan from U.S. $500 million to U.S. $600 million, on the condition that USSC grant a security interest in favour of USS in respect of its inventory of iron ore pellets sold to it by SHC. The Second Revolver Amendment did not otherwise amend the provisions of the Revolver Loan Agreement as it existed on January 28, 2013, including the events of default and consequences of a default.

[52] In furtherance of the provisions of the Second Revolver Amendment, USSC granted a security interest in favour of Credit Corp over all of its inventory of iron ore pellets sold to USSC by SHC, and related proceeds, pursuant to a security agreement dated January 28, 2013 executed by USSC and USS (the "Security Agreement").

[53] In February 2013, USS determined that the foreign currency exchange fluctuations on the Revolver Loan, which was a U.S. dollar-denominated loan, had become unacceptable as a result of the volatility of USSC's revenues, and accordingly of its quarterly earnings, due to fluctuations in the Canadian dollar. Over a period of several months thereafter, Canada LP injected significant amounts of equity into USSC to provide for USSC's working capital funding needs and to allow USSC to pay down the Revolver Loan.

[54] Between February and September 2013, as set out above, equity injections provided to USSC totaled over $680 million. Payments of principal and interest on the Revolver Loan over the same period totaled over U.S. $390 million. As of October 30, 2013, the amount outstanding under the Revolver Loan had been reduced to $116,969,996.

[55] On October 30, 2013, Credit Corp and USSC executed the Third Revolver Amendment. The Third Revolver Amendment contains a recital to the effect that the parties wish to amend and restate the Revolver Loan "in order to permit the Borrower to access the remainder of the [Revolver] Loan." The Third Revolver Amendment continued the availability under the Revolver Loan in the amount of U.S. $600 million. However, it divided borrowings under the facility into two tranches: (1) the "First Tranche Indebtedness", being the outstanding amount of $116,969,996, which was entitled to the security interest over iron-ore pellets constituted by the Security Agreement; and (2) the "Second Tranche Indebtedness", being any advances after October 30, 2013, which were entitled to the general security interest constituted by the October Security Agreement (as defined below). The Third Revolver Amendment did not otherwise amend the provisions of the Revolver Loan as it existed on October 30, 2013, including the events of default and consequences of a default.

[56] Concurrently with the execution of the Third Revolver Amendment, USSC and Credit Corp executed an amendment and restatement of the Security Agreement pursuant to an agreement also dated October 30, 2013 (the "October Amendment"). Pursuant to the October Amendment, USSC granted a general security interest over all of its personal property in favour of Credit Corp. The October Amendment contained a recital to the effect that Credit Corp "is willing to continue to provide Loans pursuant to [the Revolver Loan], only if [USSC] enters into this Amendment". The General Security Agreement, as amended by the October Amendment, is herein referred to as the "October Security Agreement". Apart from broadening the security interest granted in favour of Credit Corp, the October Amendment did not otherwise amend the provisions of the Security Agreement as it existed as of October 30, 2013.

[57] USS has acknowledged that, as of October 30, 2013, although USSC was meeting its obligations as they fell due, the total liabilities of USSC exceeded the market value of its assets and, accordingly, USSC was otherwise "insolvent", including for the purposes of section 95 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "BIA").

[58] After the execution of the Third Revolver Amendment and the October Security Agreement, Credit Corp advanced loans to USSC under the Revolver Loan totaling U.S. $71 million. These loans were outstanding at the Filing Date. USSC did not make any payments of either principal or interest after October 30, 2013 in respect of the First Tranche Indebtedness under the Revolver Loan outstanding as of October 30, 2013.

[59] Accordingly, at the Filing Date, the total amount outstanding under the Revolver Loan, including accrued interest, was U.S. $193,089,318. The portion of this balance attributable to advances made prior to October 30, 2013, i.e., to the First Tranche Indebtedness plus accrued and unpaid interest thereon since that date, was U.S. $120,150,928. This is the amount of the USS unsecured claim in respect of the Revolver Loan. The portion attributable to advances made after October 30, 2013, i.e., to the Second Tranche Indebtedness, was U.S. $72,938,390, representing U.S. $71 million of advances plus interest. This is the amount of the USS secured claim in respect of the Revolver Loan.

Internal Procedure for Additional Draws and Equity Capital Contributions

[60] In order to request funding under the Term Loan after December 31, 2007 and under the Revolver Loan, USSC would prepare and submit to USS a cash flow forecast setting out its

anticipated cash requirements for the following 13-week period. The submission of these weekly cash flow forecasts, and the related correspondence and discussions between USS and USSC, constituted USSC's formal request for funding.

[61] USS would review the forecast and determine whether funds would be advanced, and if so whether they would be advanced as debt under the Loans or as an equity injection. Typically the funds would be advanced as debt unless additional debt would cause USSC to go offside the "thin capitalization" tax rules under the *Income Tax Act*.

[62] There is no dispute that all advances made under the Term Loan were documented and recorded by both Canada LP and USSC as debt and that all advances made under the Revolver Loan were similarly documented and recorded by both Credit Corp and USSC as debt. It is also not disputed that all contributions to equity by Canada LP were recorded by both Canada LP and USSC as equity. In this regard, the Monitor has noted that USSC's books and records relating to these intercompany transactions are well organized and documented, including with respect to each specific advance of cash in the form of equity or debt.

[63] The following table summarizes the equity capital injections by USS into USSC between October 31, 2007 and the Filing Date:

Equity Contributions (CAD $Millions)

Period	Original Contribution	Equity Advances	Total
Oct 31, 2007	600		600
Nov 30, 2007	-	-	600
Dec 31, 2007	-	20	620
2008	-	55	675
2009	-	61	736
2010	-	612	1,347
2011	-	213	1,561
2012	-	-	1,561
2013	-	764	2,325
Sept 15, 2014	-	-	2,325
Total	**600**	**1,725**	**2,325**

Source: USSC Share Consideration Registry

[64] The Remaining USS Secured Claims USS has asserted the following three Claims, which it says are secured pursuant to the November Security Agreement (as defined below):

Claim	Amount (USD)	Claim Reference #
Secured Cliffs Transaction	$14,538,462.95	11(a)
Secured Credit Support Payments	$3,742,478.78	11(b)
Secured Intercompany Goods & Services	$31,252,193.05	11(c)

As mentioned, these Claims are collectively referred to as the "USS Remaining Secured Claims". It is my understanding that the Objecting Parties do not challenge the quantum of these

Claims but assert that the security for these Claims is unenforceable on the grounds described later in these Reasons.

Secured Cliffs Transaction (Claim #11(a))

[65] USS filed a secured claim for U.S. $14,538,462.95 with respect to the amount of a payment made by USS to Cliffs Natural Resources and Cliffs Sales Company (collectively, "Cliffs") for certain iron ore delivered by Cliffs to USSC, which iron ore was, in turn, resold by USS to USSC under the following circumstances.

[66] Cliffs and USS are parties to an agreement dated January 1, 2008 for the supply of iron ore (the "Cliffs Agreement"). The iron ore delivered by Cliffs to USSC was sourced by the USS Procurement Department as part of the raw materials services arrangement between USS and USSC that was provided for in the "Limited Risk Distributor Agreement" referred to below.

[67] The Claim relates to four shipments of iron ore, and associated screening charges, totaling U.S. $14.1 million, which were delivered by Cliffs to USSC in August 2014, prior to the Filing Date and outstanding obligations in the amount of U.S. $0.4 million for screening charges incurred in January and May 2014 for which Cliffs had not previously issued invoices.

[68] On September 16, 2014, pursuant to an agreement between USS and USSC (the "Iron Ore Agreement"), in order to avoid an interruption of the supply of a critical raw material under the Cliffs Agreement, USS agreed to make the payment to Cliffs and to transfer title of the iron ore pellets to USSC provided that USSC confirmed the corresponding obligation of USSC to USS in payment of such iron ore would be secured under the November Security Agreement.

[69] The Monitor has confirmed that USSC received delivery of the iron ore prior to the Filing Date and that USS made the payment of $14.1 million to Cliffs on October 2014. The Monitor has also confirmed that, under the Cliffs Agreement, title to the iron ore did not pass to USS until USS paid for the iron ore after the Filing Date. At that time, USS effectively took title to the iron ore and re-sold it to USSC pursuant to the Limited Risk Distributor Agreement described below.

[70] Accordingly, this Claim is a claim of USS for the payment of goods sold by USS to USSC after the Filing Date pursuant to arrangements set out in the Iron Ore Agreement that were entered into prior to the commencement of these proceedings under the CCAA.

Secured Credit Support Payments - Claim #11(b)

[71] USS filed a secured Claim for U.S. $3,703,450 for contribution and indemnity as guarantor of certain USSC obligations as follows:

Vendor	Amount (USD)
Independent Electricity System Operator ("IESO")	$2,616,156.27
Union Gas Limited ("Union Gas")	$669,109.87
Norfolk Southern Corporation ("Norfolk")	$457,212.64

[72] USS received demands subsequent to the Filing Date from IESO, Union Gas and Norfolk pursuant to existing guarantee agreements between USS in favour of each of such parties in respect of goods and services supplied to USSC prior to the Filing Date. USS made payments to these vendors pursuant to these guarantees subsequent to the Filing Date. This Claim is therefore an aggregation of USS' rights of subrogation which arose on payment of these three obligations of USSC after the Filing Date pursuant to the USS guarantees in favour of the third parties.

Secured Intercompany Goods & Services - Claim #11(c)

[73] In the ordinary course of business, the USS Affiliates provided raw materials and other goods as well as various services to USSC both informally and under several intercompany agreements. Invoices relating to the intercompany goods and services received by USSC in a calendar month were typically paid on a gross basis on or about the 15th day of the following month as part of a normal reconciliation process between USSC and USS.

[74] USS filed a secured claim totaling U.S. $31,252,193.05 in respect of the sale of goods and the provision of services on an intercompany basis after the date of the November Security Agreement.

[75] As stated above, the sale of goods and the provision of services by USS to USSC took place both informally and under several intercompany agreements. The relevant intercompany agreements include the following: (1) two Marketing, Distributorship and Supply Agreements, dated March 1, 2009 and December 1, 2008, which governed cross-border sales within the USS group, i.e., the sale of steel produced in the U.S. or Canada and sold to a customer in the other country; (2) a Limited Risk Distributor Agreement, dated February 1, 2008, between USS and USSC under which USSC purchased significant quantities of raw material on an as-needed basis from USS; (3) an ERP Cost Sharing Agreement, amended January 1, 2011, that governed the costs of an enterprise-wide financial and operational software solution known as "Oracle"; (4) a Corporate Services Agreement, dated November 1, 2007, pursuant to which USS provided, among other things, financial and accounting, corporate strategic planning, tax planning and audit services to USSC; and (5) a Business Services Agreement, dated January 1, 2014, among USS, USSC and USS Kosice that related to certain IT and financial transaction processing services.

[76] The claims that are aggregated as Claim #11(c) are therefore contractual claims of USS for payment of the goods and services provided pursuant to these agreements prior to the Filing Date.

Procedural History of this Proceeding

[77] Pursuant to a claims process order of the Court in these CCAA proceedings dated November 13, 2014 (the "Claims Process Order"), creditors of USSC were required to file Proofs of Claim (as defined in the Claims Process Order) in respect of affected Claims with the Monitor by December 22, 2014.

Actions of the Monitor under the Claims Process Order

[78] With respect to any claims filed by USS, U.S. Steel Holdings, Inc., Canada LP or any affiliates of USS (other than USSC or any of USSC's subsidiaries), paragraph 28 of the Claims Process Order ordered:

(a) the Monitor to prepare a report to be served on the Service List and filed with the Court, detailing its review of all USS claims and recommendations it has, if any, with respect to the determination of such claims;

(b) the Monitor to seek a scheduling appointment before the Court, on notice to the Service List, to schedule a hearing of a motion to determine the USS claims; and

(c) that the USS claims shall not be accepted or determined as Proven Claims without approval of this Court.

[79] USS and its subsidiaries and affiliates filed 14 Proofs of Claim with the Monitor, being the "USS Claims".

[80] On March 10, 2015, the Monitor issued its Seventh Report in these CCAA proceedings dated March 9, 2015 (the "Monitor's Seventh Report").

[81] As described at paragraph 8 of Monitor's Seventh Report, the USS Claims may be summarized and aggregated into the following three categories:

(a) non-contingent Secured Claims (as defined in the Claims Process Order), which total U.S. $122,432,496.11 (being the "USS Secured Claims");

(b) unsecured Claims, which total U.S. $127,805,815.36 (being Claims #1 to 8, #10 and an unsecured portion of Claim #11) and $1,847,169,934.04 (being Claim #9); and

(c) contingent Secured Claims, which total $78,761,395.00 (which are not addressed in these Reasons).

[82] The review process undertaken by the Monitor (and in certain cases by the Monitor's counsel) of the USS Claims is described at paragraphs 36-40 of the Monitor's Seventh Report. Based on its review of the USS Claims, the Monitor recommended to the Court that:

(a) USS bring a motion to approve the USS Secured Claims and the USS Unsecured Claims; and

(b) the USS Secured Claims and the USS Unsecured Claims be found to be Proven Claims in their entirety as filed by USS.

[83] Based on the Monitor's recommendations to the Court, USS commenced this proceeding by a notice of motion dated March 13, 2015. Pursuant to this motion, USS seeks to have the USS Secured Claims and the USS Unsecured Claims approved by the Court as Proven Claims pursuant to the Claims Process Order.

The Objections of the Province, the Union and Representative Counsel

[84] The following briefly summarizes the claims set out in the Objections of the Objecting Parties that have given rise to this trial. In addition, an objection was filed by Robert and Sharon Milbourne (collectively, the "Milbournes"). However, the Milbournes chose not to participate in the hearing of this motion. The Court has therefore treated their objection as withdrawn.

The Objection of the Province of Ontario

[85] On April 14, 2015, an Objection was filed on behalf of the Province.

[86] The Province submitted that the facts of this case raise significant issues with respect to the validity and enforceability of the security interests underlying the secured portions of the USS Claims as well as the proper characterization of the USS Claims. It argued that, in light of these issues, there was an insufficient basis on which to accept the USS Claims as Proven Claims. It argued that a hearing was required to evaluate these issues, which evaluation should include a consideration of whether the security claimed by USS was valid and enforceable given, among other matters, that the adequacy of consideration received by USSC in exchange for the grant of security has not been established. The Province also submitted that the Court should consider whether the USS Claims constitute *bona fide* indebtedness, or whether they are properly characterized as equity contributions from a controlling parent company.

[87] The Objection of the Province was supplemented by a clarification dated August 21, 2015, which set out in greater detail the bases upon which the Province asserts that the Term Loan and the Revolver Loan should be re-characterized as "equity claims" and that the security for the USS Secured Claims should be declared to be a fraudulent preference or otherwise unenforceable. As these arguments are addressed below in the Court's analysis, I do not propose to repeat them in this section.

The Objection of the Union

[88] On April 14, 2015, an Objection was filed by the Union. By way of overview, the Union submitted that USS, as the shareholder of USSC, directed the operations of USSC in a manner that has caused USSC to significantly underperform, thereby incurring substantial losses and requiring it to incur significant debt. In addition, the Union submitted that such actions undermined the ability of USSC to meet its on-going funding obligations to the USW pension plans of USSC. The Union argued that, as a result, USS has diluted the potential recoveries of the Union members and the USW pension plan beneficiaries in this CCAA proceeding.

[89] The Union broadly categorized its objections as follows:

(a) an objection to the granting of security interests on the assets of USSC;

(b) an objection to the characterization of most of the USS Claims as debt when they are properly characterized as equity; and

(c) an objection grounded in USS' conduct in relation to its Canadian plants, unionized pensioners, pension plan members and beneficiaries, which gives rise to claims of oppression and breaches of fiduciary duty.

[90] With respect to the objection in (a), the Union submitted that USS' secured claim is based on security interests effectively granted by USS to itself, at a time when there was no independent board of directors or advisors, for insufficient consideration, and in a manner which amounted to an improper preference and/or fraudulent conveyance. With respect to the objection in (b), the Union submitted that a significant portion of USS' debt is really in the nature of equity and should be re-characterized as such based on, among other factors, the fact that (i) much of the debt was incurred to acquire Stelco; (ii) USS completely controlled USSC; (iii) USS was the sole source of USSC's financing; (iv) USS provided commercially unreasonable interest and repayment terms; (v) USS had no reasonable expectation of repayment on the purported loans; and (vi) USSC was significantly undercapitalized throughout the years following its acquisition by USS.

[91] The first two claims of the Union overlap significantly, if not completely, with the arguments raised by the Province in its Objection. The remaining claims are not being addressed on this motion. The process for addressing such claims was the subject of an earlier hearing and the Court's endorsement that was released as *U.S. Steel Canada Inc. (Re)*, 2015 ONSC 5103.

The Objection of Representative Counsel

[92] On April 14, 2015, an Objection was filed also filed by Representative Counsel for all non-USW active employees and retirees of USSC. In its Objection and at the trial in this proceeding, Representative Counsel adopted the particulars of the Objections filed by the Province and the Union as applicable to the non-USW active employees and retirees of USSC.

The Disputed USS Claims

[93] For completeness, the Objections that were made in respect of Claims #1-5 in the Monitor's Seventh Report, which are unsecured claims in the aggregate amount of U.S. $3,085,746, have now been withdrawn by the Objecting Parties. Further, no Objections have been made in respect of Claims #6-8 in such Report, which are unsecured claims in the aggregate amount of U.S. $338,169. Therefore, based on the Monitor's Seventh Report, Claims #1-8 inclusive should be confirmed as Proven Claims. The USS Claims which are the subject of this motion, and in respect of which the Objections are maintained, are the following:

Claim Reference #	Description of Claim	Amount of Claim
9	Unsecured Term Loan	$1,847,169,934
10	Unsecured Revolver Loan	U.S. $120,150,928
11	Secured Revolver Loan	U.S. $72,938,390
11(a)	Secured Cliffs LRD Transaction	U.S. $14,538,463
11(b)	Secured Credit Support Payments	U.S. $3,742,479
11(c)	Secured Intercompany Trade	U.S. $31,252,193

[94] For clarity, none of the parties object to the quantum of the USS Claims which are the subject of the present motion.

[95] The USS motion and the Objections were addressed collectively at a trial conducted over eight days. The evidence adduced at the trial consisted of affidavit evidence and oral testimony, the relevant portions of which are described below.

Applicable Statutory Law

[96] The following provisions of the CCAA are relevant for the Objections that the USS Claims should be re-characterized as "Equity Claims" for the purposes of these CCAA proceedings:

> 2. In this Act,
>
> "Claim" means any indebtedness, liability or obligation of any kind that would be a claim provable within the meaning of section 2 of the *Bankruptcy and Insolvency Act*;
>
> "Equity Claim" means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
>
> (b) a return of capital,
>
> (c) a redemption or retraction obligation,
>
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or

> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);
>
> "Equity Interest" means
>
> (a) in the case of a corporation other than an income trust, a share in the corporation -- or a warrant or option or another right to acquire a share in the corporation -- other than one that is derived from a convertible debt, and
>
> (b) in the case of an income trust, a unit in the income trust -- or a warrant or option or another right to acquire a unit in the income trust -- other than one that is derived from a convertible debt;
>
> 6. (8) No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.
>
> 11. Despite anything in the *Bankruptcy and Insolvency Act* or the *Winding-up and Restructuring Act*, if an application is made under this Act in respect of a debtor company, the court, on the application of any person interested in the matter, may, subject to the restrictions set out in this Act, on notice to any other person or without notice as it may see fit, make any order that it considers appropriate in the circumstances.

[97] The following provisions of the CCAA are relevant to the Objections that the security for the secured USS Claims, being the general security interest granted by USSC in favour of Credit Corp in the October Security Agreement and in favour of USS, United States Steel International, Inc. and SHC in the November Security Agreement, should be invalidated on the grounds of a fraudulent preference:

> 36.1 (1) Sections 38 and 95 to 101 of the *Bankruptcy and Insolvency Act* apply, with any modifications that the circumstances require, in respect of a compromise or arrangement unless the compromise or arrangement provides otherwise.
>
> (2) For the purposes of subsection (1), a reference in sections 38 and 95 to 101 of the *Bankruptcy and Insolvency Act*
>
> (*a*) to *"date of the bankruptcy"* is to be read as a reference to *"day on which proceedings commence under this Act"*;
>
> (*b*) to *"trustee"* is to be read as a reference to *"monitor"*; and
>
> (*c*) to *"bankrupt"*, *"insolvent person"* or *"debtor"* is to be read as a reference to *"debtor company"*.

[98] Section 95 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "BIA") provides as follows:

> (1) A transfer of property made, a provision of services made, a charge on property made, a payment made, an obligation incurred or a judicial proceeding taken or suffered by an insolvent person
>
> > (a) in favour of a creditor who is dealing at arm's length with the insolvent person, or a person in trust for that creditor, with a view to giving that creditor a preference over another creditor is void as against — or, in Quebec, may not be set up against — the trustee if it is made, incurred, taken or suffered, as the case may be, during the period beginning on the day that is three months before the date of the initial bankruptcy event and ending on the date of the bankruptcy; and
> >
> > (b) in favour of a creditor who is not dealing at arm's length with the insolvent person, or a person in trust for that creditor, that has the effect of giving that creditor a preference over another creditor is void as against — or, in Quebec, may not be set up against — the trustee if it is made, incurred, taken or suffered, as the case may be, during the period beginning on the day that is 12 months before the date of the initial bankruptcy event and ending on the date of the bankruptcy.
>
> (2) If the transfer, charge, payment, obligation or judicial proceeding referred to in paragraph (1)(a) has the effect of giving the creditor a preference, it is, in the absence of evidence to the contrary, presumed to have been made, incurred, taken or suffered with a view to giving the creditor the preference — even if it was made, incurred, taken or suffered, as the case may be, under pressure — and evidence of pressure is not admissible to support the transaction.

The Issues for Determination in This Proceeding

[99] There are two principal categories of Objections addressed in this proceeding: (1) that the USS Debt Claims are, in substance, "equity claims" for the purposes of the CCAA; and (2) that the security for the USS Secured Claims is either unenforceable for lack of consideration or void as a fraudulent preference under section 95 of the BIA, as incorporated into these proceedings by virtue of section 36.1 of the CCAA. These two issues will be addressed in order after first describing certain expert evidence adduced at trial by the parties.

Expert Financial Evidence

[100] The Province and USS introduced expert evidence from three financial experts who testified at trial. The following briefly summarizes the principal issues addressed in the reports and testimony of these experts. The significance of such evidence is considered below in the Court's analysis of the characterization of the Term Loan and the Revolver Loan.

The Finnerty Report

[101] The Province introduced into evidence a report dated August 21, 2015 of Dr. John Finnerty (the "Finnerty Report"). Dr. Finnerty was qualified as an expert in financial economics. Among other things, the Finnerty Report analyzed the Term Loan and the Revolver Loan against fifteen factors, described later in these Reasons and referred to as the "*AutoStyle* factors", that are used in American courts in debt re-characterization cases. It was Dr. Finnerty's opinion that, from the perspective of financial economics, the terms of the Term Loan and the Revolver Loan, and the manner in which they were implemented, are suggestive of equity rather than debt.

[102] The Finnerty Report concluded that, in respect of the Term Loan, eight of the *AutoStyle* factors are more consistent, from a financial economics perspective, with a characterization of equity, one, being the maturity date provisions and the schedule of debt service payments, is more consistent with a characterization of debt, and the remaining six factors are "indeterminate" from a financial economics perspective.

[103] The eight factors identified in the Finnerty Report as being more consistent with an equity characterization of the Term Loan are the following: (1) the interest rate provisions and the history of interest payments; (2) the inadequacy of capitalization of ABULC at the date of the acquisition; (3) the absence of security for the advances; (4) the inability of USSC to obtain similar financing from outside institutions, based upon the Hall Report described below; (5) the extent to which advances under the Term Loan were effectively subordinated to claims of outside creditors; (6) the absence of a sinking fund to provide debt repayments; (7) the "hollow" right of USS to enforce principal and interest obligations; and (8) the failure of USSC to repay the Term Loan on the due date or to seek a postponement thereof.

[104] The Finnerty Report reached a similar opinion in respect of the Revolver Loan. The Finnerty Report concludes that ten of the *AutoStyle Plastics* factors are more consistent with equity. These are the eight factors enumerated above as being more consistent with equity in respect of the Term Loan, plus: (9) the source of the debt repayments; and (10) the lengthy fixed maturity date and the schedule of debt service payments. The Finnerty Report concludes that the extent to which the advances under the Revolver Loan were used for working capital, rather than to acquire capital assets, is more consistent with a debt characterization and the remaining two factors are "indeterminate".

The Hall Report

[105] The Province also introduced into evidence a report dated August 21, 2014 of Brad Hall (the "Hall Report"), a director of Alix Partners LLC, who was qualified as an expert in institutional lending.

[106] The Hall Report concludes that a third-party lender in an arm's length transaction would not have provided financing to ABULC/USSC in the amounts and on the terms provided by USS pursuant to the Term Loan and pursuant to the Revolver Loan. The Hall Report was incorporated into, and relied upon, by Dr. Finnerty in the preparation of the Finnerty Report.

[107] These conclusions in the Hall Report are based on an assessment of the terms of the Term Loan and the Revolver Loan against the standard of a bank or other institutional lender

offering unsecured term loans and unsecured revolving loans (herein referred to as a "third-party lender").

[108] In the opinion of Mr. Hall, a third-party lender would have based any term loan granted to USSC in 2007 on the historical financial performance of Stelco, rather than on the projections relied upon by USS for the purposes of the Acquisition, and would have disregarded any of the synergies projected by USS. In addition, a third-party lender would not have granted a term loan on an unsecured basis, nor would it have been prepared to accept the provisions of the Term Loan in respect of the maturity date, principal repayments or interest payments.

[109] Similarly, Mr. Hall was of the view that a third-party lender would not have granted an unsecured loan in the amount of the Revolver Loan in 2010 nor would it have accepted the provisions of the Revolver Loan respecting the maturity date or interest payments. In addition, the Hall Report addresses the financial performance covenants that a third-party lender would typically require, principally debt/equity, Debt/EBITDA and EBITDA/interest tests, and observed that, given USSC's financial performance after 2008, USSC would not have complied with the latter two tests as typically applied at the time of advances under the Revolver Loan.

[110] The Hall Report also concluded that the terms of the Term Loan were not comparable with the loans provided by the prior arm's length lenders to Stelco or by the arm's length lenders that provided financing at or about the same time to USS. I do not find these opinions of assistance with respect to the issues in this proceeding.

The Austin Smith Report

[111] USS introduced into evidence a report dated September 4, 2015 of Yvette R. Austin Smith (the "Austin Smith Report"), a principal of the Brattle Group, which addressed certain features of the Finnerty Report and the Hall Report. For present purposes, the Austin Smith Report reached three principal conclusions, aspects of which are relevant for the determinations below in these Reasons.

[112] First, the Austin Smith Report says that the conclusions in the Finnerty Report — that, from a financial economics perspective, the terms of the Term Loan and the Revolver Loan, and the manner of their administration, are strongly suggestive of an equity investment — relies too heavily on hindsight to be credible. The Report suggests that, as a result, the application of the *AutoStyle* factors does not assist in establishing the substance of these transactions or the intent of the parties at the time of the establishment of the Loans.

[113] Second, the Austin Smith Report concludes that the opinion in the Hall Report that USSC could not have financed the Term Loan and the Revolver Loan "in the amounts and on the terms as provided by USS" relies on a flawed credit analysis of USSC that, therefore, does not address USSC's debt capacity after the Acquisition.

[114] Third, the Austin Smith Report suggests that the opinions in the Hall Report, and therefore in the Finnerty Report, ignore the reality of diverse corporate debt markets in their concentration on the third-party lender market.

Observations Regarding the Expert Financial Evidence

[115] I do not propose to make any finding regarding the differences of opinion expressed in the Finnerty Report and in the Austin Smith Report on the particular issues raised in the latter as it is not necessary to do so for the purposes of the determinations herein. However, the following three observations regarding the matters addressed in the expert evidence relied upon by the Objecting Parties are relevant to the approach set out below in these Reasons.

[116] First, in respect of most of the *AutoStyle* factors to which Dr. Finnerty refers as suggestive of equity rather than debt, Dr. Finnerty expressly or implicitly measures the Term Loan and the Revolver Loan against the standard of a bank or other institutional lender offering unsecured term loans and unsecured revolving loans, that is, against the standard of a third-party lender offering such loans.

[117] At the risk of some oversimplification, Dr. Finnerty's logic is as follows. The Term Loan and the Revolver Loan purport on their face to be an unsecured term loan and an unsecured revolver loan. The market for such loans is the third-party lender market. However, the terms and conditions of the Term Loan and the Revolver Loan are not terms and conditions that would be acceptable to a third-party lender nor were the Loans administered in certain respects in the manner that would be expected of a third-party lender. Therefore, from the perspective of financial economics, the Loans must be equity. It is the validity of the last proposition in this chain that is at issue in this proceeding. The conclusions of Dr. Finnerty are more or less relevant in this proceeding depending upon whether a third-party lender standard is appropriate in addressing financial arrangements between a parent corporation and its wholly-owned subsidiary. This issue is addressed below.

[118] Second, as Dr. Finnerty testified, of the fifteen *AutoStyle* factors, three principal factors inform his conclusions that the Loans are more suggestive of equity rather than debt. These factors are: (1) the absence of available financing from third-party lenders on the terms and in the amount of the Term Loan and the Revolver Loan; (2) the waiver of interest payments under the Term Loan in 2010 and thereafter; and (3) the "fungibility of debt and equity", which refers to the payment of interest and repayment of principal by USSC out of equity injections received from USS, principally in respect of the Revolver Loan. It is therefore appropriate to focus on the evidentiary value of these three considerations, rather than on the larger list which effectively repeats the same considerations.

[119] Lastly, I would observe that, while Dr. Finnerty was qualified as an expert in financial economics, substantially all of his expert evidence related to his view of third-party lender behaviour in various circumstances, rather than to any more formal analysis that was informed by the analytical framework of financial analysis.

Expert Legal Evidence

[120] USS and the Province also introduced expert legal evidence from two lawyers who testified at trial regarding a specific issue of Pennsylvania law. The following briefly summarizes the issue of law and the testimony of these experts. The issue is significant for the analysis of the validity of the security for the USS Secured Claims.

The Issue

[121] The Revolver Loan Agreement contained an event of default in section 11c as follows: "Borrower consents to the appointment of a receiver, trustee or liquidator of all or substantially all of its assets, is unable to meet debts, or files bankruptcy". The same event of default was continued after each of the First Revolver Amendment, which removed the solvency representation, the Second Revolver Amendment and the Third Revolver Amendment.

[122] The expert testimony addressed the meaning of the phrase "unable to meet debts" as a matter of contractual interpretation under the laws of Pennsylvania. Both experts testified that the principles of contractual interpretation under Pennsylvania law are substantially similar to the principles under Ontario law with, based on USS' expert, a tendency toward somewhat greater emphasis on the strict construction of contracts.

[123] I would observe that, while the expert testimony was tendered in respect of this provision in the Revolver Loan Agreement, the same event of default appears in section 13(c) of the Term Loan Agreement which is governed by the laws of Alberta.

The McMichael Report

[124] USS introduced into evidence a report dated August 21, 2015 of Lawrence McMichael (the "McMichael Report"). It was Mr. McMichael's opinion that the phrase "unable to meet debts" connoted a balance sheet solvency test which, under Pennsylvania law, would be performed on a market value basis. Accordingly, Mr. McMichael was of the opinion that the contractual interpretation of clause 11c of the Revolver Loan Agreement resulted in an event of default in the circumstances in which the aggregate liabilities of USSC exceeded the fair market value of its assets.

The Di Massa Report

[125] The Province introduced into evidence a report dated September 4, 2014 of Rudolf Di Massa, Jr. (the "Di Massa Report"). It was Mr. Di Massa's opinion that the phrase "unable to meet debts" did not connote an insolvency test as such, whether on a balance sheet basis or on a going concern basis. Mr. Di Massa was of the view that the correct statutory interpretation of this phrase meant "unable to satisfy or manage its obligations relating to operating activities on an on-going basis given its financial resources from all available sources". He described this event of default as essentially a direction from USS to USSC to manage its financial obligations by obtaining credit from all available sources, including from trade creditors through an extension of payment terms and from USS itself by drawing up to the maximum availability under the Revolver Loan Agreement.

[126] An important feature of Mr. Di Massa's interpretation is his view of the operation of the Revolver Loan Agreement, which is significant in three respects. Mr. Di Massa's opinion implies that an event of default would not arise unless and until USSC had drawn the maximum availability under the Revolver Loan Agreement and was unable to foresee obtaining credit from any other possible sources on a prospective basis. It also implies that, under the Revolver Loan Agreement, USS was obligated to continue to advance funds until such maximum availability was reached, subject to the occurrence of one of the other events of default in the Agreement.

Lastly, as the phrase "unable to meet debts" is the only event of default that appears to address the state of insolvency, and, as Mr. Di Massa is of the view that this phrase does not serve as an insolvency event of default, his interpretation has the result that the Revolver Loan Agreement lacks an express insolvency event of default.

The Findings of the Court

[127] The Court finds that, under the laws of Pennsylvania, the words "unable to meet debts" in the Revolver Loan Agreement mean that the fair market value of the assets of USSC are less than the total of its liabilities, that is, that the words connote a balance sheet solvency test. I reach this conclusion for the following four reasons.

[128] First, this interpretation is more consistent with the plain meaning of the words "unable to meet debts" than the interpretation proposed by Mr. Di Massa. In particular, it recognizes the absence of the additional words "when due", or words to a similar effect. Such words appear in the events of default in sections 11a and 11b of the Revolver Loan Agreement. If they had been incorporated into the "unable to meet debts" event of default, I think it is clear that they would have indicated an intention to apply an event of default in the event of an inability to meet USSC's obligations as they fell due, i.e. a going concern event of default. Their absence indicates an intention that the event of default would relate to the alternative definition of insolvency under the laws of Pennsylvania, being the extent of assets relative to liabilities. For this reason, while it is true that the parties could have used more specific language if they had intended a balance sheet insolvency event of default, instead of the rather archaic phrase that appears, I do not think that such words connote a going concern event of default or the approach proposed in the Di Massa Report.

[129] Second, as a related matter, the interpretation proposed in the Di Massa Report requires reading in language that is neither present nor customary. Such an interpretation should be rejected in favour of an interpretation that gives effect to the plain meaning of the language of the event of default.

[130] Third, even assuming an ambiguity in the language of the event of default, the Di Massa Report relies heavily on an inference based on the removal of the solvency representation from the Revolver Loan agreement by the First Revolver Agreement. The solvency representation spoke to both balance sheet solvency and solvency on a going concern basis. It is suggested that it would have been illogical for USS and USSC to have removed the solvency representation and maintained a balance sheet event of default. It is also suggested that interpretation of the event of default as a balance sheet solvency event of default would have resulted in a continuing state of default under the Revolver Loan Agreement, with automatic acceleration of the Revolver Loan, which could not have been intended.

[131] As discussed later in these Reasons, I do not think that any conclusion can be drawn regarding the intention of the parties in respect of the removal of the solvency representation. In particular, I do not think that there is any evidence regarding the surrounding circumstances in which the First Revolver Amendment was negotiated and executed that bears on the interpretation of the event of default.

[132] Fourth, an important principle of contractual interpretation is that, in the case of ambiguity, a court should prefer the more commercially reasonable interpretation. In my view, for the following reasons, the interpretation proposed by Mr. Di Massa results in an unreasonable result from a commercial perspective.

[133] In this case, while the interpretation in the McMichael Report may have had the result that USSC was in default as of the execution of the Third Revolver Amendment, if not before, I do not see a particular difficulty in this. Unlike a third-party lender, there is no evidence that USS had a particular concern with the occurrence of a balance sheet event of default under the Revolver Loan. It could always choose to waive any event of default and advance further funds notwithstanding the occurrence of an event of default. In this respect, the evidence of Mr. Di Massa that a commercial lender would not engage in such behaviour is not a relevant consideration.

[134] On the other hand, USS would have had a significant concern with any renunciation of its ability to control the extent, if any, of future advances of funds. As Mr. McMichael testified, lenders, including parents of wholly-owned subsidiaries, do not intend to be bound to lend money that they do not believe will be repaid. This is particularly important with respect to the operation of the Revolver Loan Agreement in October 2013 given the amount of the undrawn facility — being approximately U.S. $383 million — and the cash burn of USSC in 2013, including the anticipated cash burn for the rest of the year. In addition, USS would not have intended the availability under the Revolver Loan to extend beyond what was absolutely necessary, having just completed a significant de-leveraging exercise for other reasons.

[135] Further, as noted above, the interpretation in the Di Massa Report has the result that there is no balance sheet event of default in the Revolver Loan Agreement. As a parent corporation controls the advance of funds to a subsidiary, and thereby its ability to meets its obligations on an on-going basis, a parent corporation would not necessarily need an event of default for a failure to meet on-going obligations. It would, however, require a balance sheet event of default for protection against third parties in the event of an insolvency of its subsidiary.

[136] Given the foregoing considerations, I consider that the interpretation proposed by Mr. Di Massa produces a commercial unreasonable result while the interpretation of Mr. McMichael results in a commercially viable loan arrangement.

The Debt Re-Characterization Claims

[137] I propose to address the debt re-characterization claims of the Objecting Parties in the following order. First, I will deal with two threshold issues. Next, I will address the test to be applied by the Court in the analysis of the characterization of both the Term Loan and the Revolver Loan. I will then address the debt characterization claims of the Objecting Parties in two parts. The first part addresses certain general considerations raised by the Objecting Parties that are common to both the Term Loan and the Revolver Loan. The second part sets out my analysis of each of the Term Loan and the Revolver Loan in turn in light of the Court's determinations regarding these general considerations.

Threshold Issues

[138] The two threshold questions to be addressed are: (1) the onus of proof; and (2) the test to be applied in the evaluation of the debt re-characterization claims respecting the USS Debt Claims. I will address each issue in turn.

The Onus of Proof

[139] As would be expected, USS argues that the burden of proof lies with the Objecting Parties and the Objecting Parties argue that it lies with USS. I will deal separately with the burden of proof pertaining to the debt re-characterization claims of the Objecting Parties and the claims that the security for the USS Secured Claims is invalid or otherwise unenforceable.

[140] The issue of the burden of proof in respect of the debt re-characterization claims appears to be a matter of first impression as the parties have been unable to find any case law on this issue. I conclude that the Objecting Parties have the burden of proof that the USS Debt Claims are properly characterized as "equity claims" under the CCAA for the following three reasons.

[141] First, in a claims process under the CCAA, a creditor bears the onus of proving the validity and amount of its debt claim. It is not required to go further and prove the negative. In other words, it does not have to demonstrate that a claim is not an "equity claim". If another creditor chooses to assert such an argument, I think it must bear the onus of proving that an otherwise proven debt claim is more properly characterized in substance as an "equity claim".

[142] Second, put in procedural terms, the motion of the creditor, in this case USS, is limited to a determination of the validity and amount of its debt claim in order to establish a "Proven Claim" under the Claims Process Order. The objection of any other creditor, in this case the Objecting Parties, is in substance a cross-motion for a declaration that the debt claim, if accepted, constitutes in substance an "equity claim" for the purposes of the CCAA. I do not agree with the Objecting Parties that the motion of the objecting creditor should be regarded as the substantive equivalent of a statement of defence which must be addressed to establish the validity and amount of a moving party's debt claim.

[143] Lastly, an important consideration is that the debt re-characterization claims of the Objecting Parties are based on the underlying substantive reality of the Term Loan and the Revolver Loan. These are factual matters, rather than matters based on allegations of inequitable behavior on the part of USS. I accept that there may be an argument for a reversal of the onus of proof in the circumstances of a *bona fide* allegation of bad faith or inequitable conduct on the part of an insider or a controlling shareholder of a debtor company that could engage an equitable remedy in favour of the injured party or an analogous statutory remedy. However, as mentioned, that is not the basis of the claims of the Objecting Parties on this motion.

[144] The Objecting Parties' argument that the security for the USS Secured Claims is invalid or, in the alternative, unenforceable raises two issues, although I conclude that the Objecting Parties bear the onus of proof in either case.

[145] With respect to the claim that the October Security Agreement and the November Security Agreement are unenforceable for lack of consideration, I think the same principles govern the issue of onus as apply with respect to the issue of onus regarding the treatment of the USS Debt Claims as "equity claims". A creditor asserting a Secured Claim must move for a determination that the security is valid. To such end, the creditor must establish that the security was delivered by the debtor company, that the security is expressed to cover the creditor's claim, and that any necessary registrations were effected under applicable legislation. An objection of any other creditor that such security is invalid or otherwise unenforceable on any other basis would involve a cross-motion by such objecting creditor seeking a declaration to such effect.

[146] With respect to the claim that the October Security Agreement and the November Security Agreement constitute fraudulent preferences for purposes of section 95 of the BIA, the Objecting Parties acknowledge that the case law establishes that they bear the onus of proof.

The Test to Be Applied

[147] The more difficult threshold issue is identification of the test to be applied to determine whether the USS Debt Claims are debt obligations or "equity claims".

[148] The Term Loan and the Revolver Loan are, on their own terms, loans rather than equity contributions. The terms and conditions of the Term Loan Agreement and the Revolver Loan Agreement unequivocally evidence loan agreements. The Term Loan and Revolver Loan are both documented as loans in contracts entitled "Loan Agreement" in which the parties are described as lender and borrower. Each loan agreement prescribes a term and an interest rate, requires repayment, and has no terms expressly tying any payments to the financial performance of USSC. USS and USSC also had very different processes for approval and transmission of loan advances and equity contributions. The financial accounts of Canada LP or Credit Corp, as applicable, and USSC accurately recorded the loan advances separately from equity contributions.

[149] The form of the documentation for the Loans, and the foregoing actions, are the point of departure. USS says it intended the outstanding advances under the Term Loan and the Revolver Loan to be loans rather than capital contributions. Accordingly, USS says that the USS Debt Claims are in respect of loans and are not "equity claims". The issue for the Court on this motion is, therefore, whether the foregoing actions and documentation are determinative. USS argues that there is no further issue for the Court for two alternative reasons based, respectively, in the language of the CCAA and in the pre-2009 Canadian case law. I will address these two arguments in turn.

The Provisions of the CCAA

[150] USS argues that the most recent amendments to the CCAA, which introduced the definition of "equity claims", comprehensively codified the treatment of "equity claims" with the result that the issue of whether a particular claim is to be treated as debt or equity is solely a matter of statutory interpretation. It relies on *Re Sino-Forest Corp*., 2012 ONCA 816, 114 O.R. (3d) 304, at paras. 30 and 36, for this proposition.

[151] In the circumstances of this case, USS argues that the USS Debt Claims are not claims in respect of a share of USSC, or a warrant or option or another right to acquire a share of USSC. It submits that, accordingly, the USS Debt Claims are not claims in respect of an "equity interest" and, therefore, are not "equity claims". USS says that, as a result, the USS Debt Claims are claims in respect of loans.

[152] I agree that the issue of whether a particular claim is to be treated as debt or equity is a matter of statutory interpretation. I also agree that the USS Debt Claims do not fall within paragraph (d) of the definition of "equity claim" which refers to "a monetary loss resulting from the ownership, purchase or sale of an equity interest". This provision addresses the circumstances of shareholders pursuing securities misrepresentation or oppression actions against a debtor company. It prevents recovery of claims by such shareholders for the value paid for their shares prior to the satisfaction of claims of debt-holders of the debtor company: see *Re Sino-Forest Corp*., 2012 ONSC 4377 (Commercial List), at paras. 71, 80, 96, aff'd 2012 ONCA 816, 114 O.R. (3d) 304.

[153] However, I do not read the definitions of "equity claim" and "equity interest" as narrowly as USS. The USS argument relies implicitly on the need for the demonstration of the issuance of shares as a requirement of an "equity claim". In doing so, USS ignores the reality of a sole shareholder situation and reaches an unreasonable conclusion.

[154] In the circumstances of a sole shareholder, there is no practical difference for present purposes between a shareholding of a single share and a shareholding of multiple shares. Accordingly, for the purposes of the definition of an "equity claim", there should be no difference between a payment to a debtor company on account of the issuance of new shares and a payment to a debtor company by way of a contribution to capital in respect of the existing shares.

[155] On this basis, I conclude that, as a matter of statutory interpretation, the definition of an "equity claim" must extend to a contribution to capital by a sole shareholder unaccompanied by a further issue of shares. Put another way, I conclude that a payment by a sole shareholder of a debtor company on account of a capital contribution constitutes a payment in respect of a share of the debtor company. Such a payment would therefore constitute an "equity interest" and a claim in respect of such payment in a CCAA proceeding would be a claim for a return of such capital and therefore an "equity claim".

[156] Further, I conclude that there is no reason why the reference to "a return of capital" in paragraph (b) of the definition of "equity claim" should be limited a claim in respect of an express contribution to capital by a shareholder. A transaction can be a contribution to capital in substance even if it expressed to be otherwise.

[157] Accordingly, I conclude that the issue for the Court in this proceeding is whether the USS Debt Claims constitute claims for a return of capital in respect of the shares in USSC owned by USS. In order to decide that issue, the Court must decide whether the advances made under the Term Loan and the Revolver Loan constituted loans to USSC or contributions to the capital of USSC in respect of the outstanding shares of USSC owned by USS. To the extent any of such advances constituted a contribution to capital, any claim for such amounts as Proven Claims in

these CCAA proceedings would constitute a claim for a return of capital and, therefore, an "equity claim".

Pre-2009 Canadian Case Law

[158] USS makes an alternative submission in the event the Court finds that the definition of "equity claim" does not preclude a determination of whether the USS Debt Claims are be treated as debt or equity. USS says that the applicable Canadian case law regarding debt re-characterization issues, which pre-dates the recent amendments to the CCAA, requires that a court have regard solely to the intention of the parties as a matter of the contractual interpretation of the relevant documentation in determining whether any transaction gave rise to an "equity interest".

[159] In this case, as mentioned above, USS says that the relevant documentation consists of the Term Loan Agreement, the Revolver Loan Agreement and the documentation pertaining to the advances and payments thereunder. USS submits that the intention of both parties at the time of execution of the Term Loan Agreement and the Revolver Loan Agreement, and at the time of all advances thereunder, is manifest on the face of such documents. It submits that, as a matter of contractual interpretation, it is clear that USS and USSC intended that such transactions would constitute debt obligations of USSC rather than capital contributions by USS to USSC. USS says that Canadian case law provides no basis for going beyond the exercise of contractual interpretation to evaluate whether the USS Debt Claims should be characterized as "equity claims" on some other basis.

[160] In making this argument, USS relies, in particular, on the decision of the Supreme Court in *Canada Deposit Insurance Corp. v. Canadian Commercial Bank*, [1992] 3 S.C.R. 558. In that decision, the issue was whether certain monies provided to the Canadian Commercial Bank (the "CCB") had been provided by way of a loan or a capital investment. At paragraph 51, the Court approached the issue before it as a matter of contractual interpretation as follows:

> As in any case involving contractual interpretation, the characterization issue facing this Court must be decided by determining the intention of the parties to the support agreements. This task, perplexing as it sometimes proves to be, depends primarily on the meaning of the words chosen by the parties to reflect their intention. When the words alone are insufficient to reach a conclusion as to the true nature of the agreement, or when outside support for a particular characterization is required, a consideration of admissible surrounding circumstances may be appropriate.

[161] The Supreme Court concluded that the transaction in that case was a loan, noting that: (1) there was nothing in the express terms of the agreements in question which supported a conclusion that the money was advanced as an investment; and (2) there were express provisions supporting a characterization of the advance as a loan, including provisions for repayment, for an indemnity should full repayment not be made from the sources contemplated, and for equal ranking with the ordinary creditors of CCB: see *Canada Commercial Bank*, supra at para. 63.

[162] In *(Re) Bul River Mineral Corporation*, 2014 BCSC 1732, 16 C.B.R. (6th) 173, Fitzpatrick J. summarized the principles in *Canadian Commercial Bank* in the following manner, which I find helpful in the present case:

> (a) the fact that a transaction contains both debt and equity features does not, in itself, determine its characterization as either debt or equity;
>
> (b) the characterization of a transaction under review requires the determination of the intention of the parties;
>
> (c) it does not follow that each and every aspect of a "hybrid" debt and equity transaction must be given the exact same weight when addressing a characterization issue; and
>
> (d) a court should not too easily be distracted by aspects of a transaction which are, in reality, only incidental or secondary in nature to the main thrust of the agreement.

This summary demonstrates that the issue before the court in *Canadian Commercial Bank* was the characterization of an instrument that had characteristics of both debt and equity.

[163] I do not find the decision of *Canadian Commercial Bank* helpful in the present circumstances for the reason that the present circumstances differ in two important respects.

[164] First, the subject-matter in *Canadian Commercial Bank* was, as mentioned, a hybrid security, i.e., a security having characteristics of both debt and equity. Therefore the issue was whether the security in question should be characterized as a debt obligation or a capital investment. The present proceeding does not involve a hybrid security. As mentioned above, the relevant documentation unequivocally evidences loan transactions on their face.

[165] Second, the parties to the transaction in *Canadian Commercial Bank* were at arm's length and the transaction documentation represented the outcome of arm's length negotiations between the parties. The parties to the Term Loan Agreement and the Revolver Loan Agreement were not at arm's length. As a result, the form of the documentation, including the characterization of the transaction as debt rather than equity, was determined by USS in its sole discretion, subject only to satisfaction of any applicable Canadian legal considerations raised by USSC.

[166] In such circumstances, the task of a court is qualitatively different from that in *Canadian Commercial Bank*. In that decision, given the hybrid nature of the security under consideration, the issue was whether the parties intended that the institutions providing financial support to the CCB were making a capital investment in the bank or were making a loan to it. In other words, the intentions of the parties were unclear without a contractual analysis to determine the substance of the transaction that had been agreed upon. At the same time, given the arm's length relationship between the parties, the language of the agreements could be relied upon as an accurate reflection of the intentions of the parties regarding the substantive reality of the transaction.

[167] Where, however, as in the present circumstances, the parties are not at arm's length, the issue is not what the parties say they intended regarding the substance of the transaction as a

matter of contractual interpretation. The expressed intention of the parties is clear. However, given the absence of any arm's length relationship, there can be no certainty that the language of the agreements reflects the underlying substantive reality of the transaction. Accordingly, the issue for a court is whether, as actually implemented, the substance of the transaction is, in fact, different from what the parties expressed it be in the transaction documentation.

[168] In other words, the task of a court is to determine whether the transaction in substance constituted a contribution to capital notwithstanding the expressed intentions of the parties that the transaction be treated as a loan. It is therefore not appropriate to limit the inquiry into the intentions of the parties to a review of the form of the transaction documentation. Such an exercise reduces to a "rubber stamping" of the determination of a single party to the transaction, i.e., the sole shareholder, and it does not address the substance of the transaction as it was actually implemented. In such circumstances, the determination of whether a particular claim is to be treated as debt or equity must address not just the expressed intentions of the parties as reflected in the transaction documentation but also the manner in which the transaction was implemented and the economic reality of the surrounding circumstances.

[169] USS also refers to the decision of the Court of Appeal in *Metropolitan Toronto Police Widows and Orphans Fund v. Telus Communications Inc.*, [2005] O.J. No. 2309 (C.A.), leave to appeal to S.C.C. denied, [2005] S.C.C.A. No. 379, at paras. 38-40. In these paragraphs, the Court of Appeal stated that: (1) the determination of the legal character of a transaction is not a simple mechanical exercise of assessing and tallying up a list of factors and then deciding whether they net out to one or the other; and (2) that a court must give legal effect to the intention of the parties as expressed in the language of an agreement. In that case, the Court of Appeal also recognized that the respective needs of the parties to an agreement are an indication of their intention and that parties are entitled to structure their contractual relationships as they see fit, absent a sham or public policy considerations dictating otherwise.

[170] I do not find this decision to be helpful in the present circumstances for the same reasons as the decision in *Canadian Commercial Bank* does not address the issues in the present proceeding. *Metropolitan Toronto Police Widows and Orphans Fund* involved the characterization of a securitization transaction as either a sale or a loan. In that context, the issue before the Court of Appeal was a matter of contractual interpretation. The transaction was an arm's length commercial transaction. Accordingly, the documentation before the court in that case could be relied upon to accurately reflect the intentions of the parties regarding the underlying economic reality of the transaction. I do agree, however, with the statement of the Court of Appeal in that decision that determination of the substantive nature of a transaction is not conducted by means of a simple "scorecard" of factors.

[171] I would observe, however, that in large measure the difference between the parties in this proceeding – which appears to reduce to the significance to be attached to the manner in which the Loans were administered – is perhaps more semantic than real. The Objecting Parties proposed, and USS accepted, that a useful summary of the appropriate approach to be taken in the present proceeding was set out in a non-binding, American decision, *In re Fedders North America, Inc.*, 405 B.R. 527 (2009), U.S. Bankruptcy Court, D. Delaware, at para. 59, as follows:

> The law regarding recharacterization is well-settled in this jurisdiction. The Third Circuit has held that the overarching inquiry with respect to recharacterizing debt

> as equity is whether the parties to the transaction in question intended the loan to be a disguised equity contribution. *In re SubMicron Systems Corp.*, 432 F.3d 448, 455-56 (3d Cir.2006). This intent may be inferred from what the parties say in a contract, from what they do through their actions, and from the economic reality of the surrounding circumstances. *Id.* at 456. Recharacterization has nothing to do with inequitable conduct, however. *See In re AutoStyle Plastics, Inc.*, 269 F.3d 726 at 748-49 (6th Cir. 2001) (discussing the differences between equitable subordination and recharacterization)

[172] On this basis, the parties do not dispute the process so much as the result. They have fundamentally different views on the intentions of USS and USSC regarding the substance of the transaction which I think can be summarized as follows.

[173] The Objecting Parties say that the Term Loan Agreement and the Revolving Loan Agreement reflect arrangements under which USS intended, at all times, on the one hand, to return excess cash to USS when it became available, and, on the other hand, to write off the principal or interest to the extent that payments of either were due and sufficient cash was not available.

[174] USS acknowledges that the Term Loan and subsequently the Revolver Loan were established with the intention of constituting the principal vehicles by which cash would be advanced to USSC, initially for the purposes of the Acquisition and subsequently for working capital purposes, and by which excess cash in USSC from any source would be repatriated to USS. USS says, however, that, at all times, it extended advances and made payments under the Term Loan and the Revolver Loan in accordance with their terms. USS argues that nothing in the manner in which it established or operated the Term Loan and the Revolver Loan reflected, in substance, a contribution to the capital of USSC, and that the only contributions to capital were made outside the loan arrangements in the form of the equity injections set out in Exhibit "O" to the Monitor's Seventh Report.

[175] These two competing views of the substance of the Term Loan and the Revolver Loan frame the debt re-characterization issues addressed in these Reasons.

The American Multi-Factor Analysis

[176] Given these competing views of the Term Loan and the Revolver Loan, it is necessary to determine an appropriate test for the determination of whether the USS Debt Claims are in substance claims in respect of loans or are "equity claims". The Objecting Parties urge the Court to adopt the multi-factor analysis prevailing in American courts under which courts evaluate a long list of factors drawing conclusions about what factors are most determinative in any given fact scenario.

[177] As referenced above, a leading case in this area is *In re AutoStyle Plastics, Inc.*, 269 F.3d at 749-50 (6th Cir., 2001), in which the court articulated the following eleven factors:

> (1) the names given to the instruments, if any, evidencing the indebtedness; (2) the presence or absence of a fixed maturity date and schedule of payments; (3) the presence or absence of a fixed rate of interest and interest payments; (4) the

> source of repayments; (5) the adequacy or inadequacy of capitalization; (6) the identity of interest between the creditor and the stockholder; (7) the security, if any, for the advances; (8) the corporation's ability to obtain financing from outside lending institutions; (9) the extent to which the advances were subordinated to the claims of outside creditors; (10) the extent to which the advances were used to acquire capital assets; and (11) the presence or absence of a sinking fund to provide repayments.

In addition, courts in other American circuits have considered the following additional factors: (1) the right to enforce payment of principal and interest; (2) participation in management flowing as a result; (3) the failure of the debtor to repay on the due date or to seek a repayment postponement; and (4) the intent of the parties: see *In re Submicron Systems Corporation*, 432 F.3d (3rd Cir., 2006), at 455-456. In the interest of simplicity, in these Reasons I refer to the fifteen factors enumerated in this paragraph as the "*AutoStyle* factors", although I acknowledge this is technically inaccurate.

[178] The Objecting Parties refer to the following description of the multi-factor analysis from *In re Submicron Systems Corporation*, at 455-456, which appears to restate the approach set out above in *Re Fedders*:

> In defining the re-characterization inquiry, courts have adopted a variety of multi-factor tests borrowed from non-bankruptcy case law. While these tests undoubtedly include pertinent factors, they devolve to an overarching inquiry: the characterization as debt or equity is a court's attempt to discern whether the parties called an instrument one thing when in fact they intended it as something else. That intent may be inferred from what the parties say in their contracts, from what they do through their actions, and from the economic reality of the surrounding circumstances. Answers lie in facts that confer context case-by-case.

[179] There does not appear to be any reported Canadian or Commonwealth cases in which courts have purported to apply the multi-factor, re-characterization tests relied upon by the Objecting Parties prevailing in American courts. The Objecting Parties urge the Court to formally adopt the foregoing eleven or fifteen factors in making a determination in this proceeding.

[180] American courts find authority for this approach in the general equitable powers granted to a bankruptcy court under the provisions of section 105(a) of the United States *Bankruptcy Code*, 11 U.S.C 1982, which is the equivalent of section 11 of the CCAA. USS says the Court lacks similar authority under the CCAA on the basis that the recent amendments to the CCAA in this area have limited the scope of a court's authority under section 11. USS relies on the earlier decision of the Court in *U.S. Steel Canada Inc. (Re)*, 2015 ONSC 5103, at para. 51, as follows:

> … I consider that the language of the definition of an 'Equity Claim" and of the provisions of section 36.1 operates as a "restriction set out in the Act" for the purposes of section 11 of the CCAA which has the effect of limiting the authority of the Court in any determination regarding an "Equity Claim" or in any proceedings brought under section 36.1.

However, that decision does not address the extent of the Court's authority under the CCAA in the evaluation of whether a security or a transaction expressed to be a debt claim is, in substance, an "equity interest". At a minimum, any such evaluation requires consideration of a number of the factors considered by American courts in the multi-factor analysis and by Canadian courts in evaluating the underlying substance of a transaction.

[181] The more immediate, and more important, issue for the Court is a framework for identification of the specific considerations or factors to be applied in the context of the present proceeding. The American cases evidence the obvious reality that, in any given situation, different factors or considerations will be more or less persuasive. Insofar as the American cases suggest a "scorecard" approach, however, I have rejected such an approach in favour of an evaluation of the substantive reality of the USS Debt Claims. In the end, in this proceeding, the *AutoStyle* factors constituted no more than the starting point, in the form of a list of factors upon which the parties drew to support their characterization of the USS Debt Claims. In short, it is not necessary to adopt the American, multi-factor analysis as a formal matter in the determination of the issues before the Court, and I therefore decline to do so.

The Approach of the Court

[182] As a first step in the identification of the specific considerations that should inform the determination of the substance of the USS Debt Claims, I propose to start with a conceptual understanding of the dividing line between debt and equity.

[183] An appropriate starting point is the definition of debt and equity for financial purposes set out in paragraphs 32 and 34 of the Finnerty Report:

> At its heart, the difference between equity and debt lies in the fundamental nature of their respective claims on the assets and cash flow of the company. Debt involves borrowing funds subject to a legal commitment to repay the borrowed money with interest at an agreed rate by a stated maturity date. This commitment is embodied in a contract, and this contract is implemented by the borrower. Lenders receive a contractually agreed set of cash flows, typically through periodic interest payments and one or more principal repayments, the last of which occur on the maturity date. … In contrast to debt, an equity claim entitles the holder to a share of the company's profits and residual cash flows after the company has made all the contractually required debt service payments. That is, the debt ranks senior to the equity with respect to the company's cash flows. Similarly, the debt ranks senior to the equity in the event the company must be liquidated and its assets sold to repay its debt obligations. The equityholders get what is left after the holders of the debt have been paid in full; if the debtholders can't get paid in full, then the equityholders get nothing.

[184] With this definition in mind, the Province suggests that the Court should address the substance of the Term Loan and the Revolver Loan from the perspective of whether the evidence is more consistent with an intention and a practice of repayment of principal plus interest under these Loans, or the payment of the residual cash flow and assets of USSC. I think this is a helpful approach, even if at a general level.

[185] Therefore, in the context of a parent-subsidiary relationship, the fundamental consideration in assessing whether a transaction is a loan is whether a holder of the instrument expects at the outset to be repaid the principal amount of the loan with interest out of cash flows of the company. The definition above implies a belief on the part of a lender that its debtor has the financial capacity to generate cash flow sufficient to pay interest and repay principal over the term of the loan, regardless of the profitability of the debtor from time to time in the course of that term.

[186] This approach suggests that the issue of whether the Term Loan and the Revolver Loan should be characterized as debt or equity can best be addressed by considering two issues: (1) the expectation of USS regarding repayment of principal with interest of the Term Loan and the Revolver Loan out of cash flows of USSC over the term of these Loans; and (2) the reasonableness of such expectation.

[187] The first of these questions addresses a subjective issue – the expectations of USS. Obviously, if, at the time of making advances under a Loan, USS had no expectation that USSC would honour any payment obligation under the Loan when due in the absence of available cash at such time and, for example, intended from the outset to waive all interest as it became payable and to forgive the principal indebtedness when it became due, the Court would disregard the form of the documentation as, in effect, a sham.

[188] The second question addresses a more objective issue assuming the existence of an expectation of repayment with interest of the Loan – the reasonableness of such expectation. This question engages, among other issues, the adequacy of capitalization of a wholly-owned subsidiary and the debt capacity of the subsidiary. If USSC were only nominally capitalized, this might be relatively easy to disprove. In this proceeding, as in most cases, however, this issue will involve, among other things, expert evidence regarding the availability of financing in capital markets generally.

[189] It is important for present purposes to note that, given that the burden of proof rests with the party asserting that a purported loan is, in substance, a capital contribution, the onus lies on the Objecting Parties, as the parties seeking to re-characterize the Loans as equity, to demonstrate that there was no reasonable basis for USS's expectations. There are good policy reasons for such a standard.

[190] Any determination of the reasonableness of a lender's expectations at the time of the making of a loan, or an advance under a loan, is prospective in nature and therefore highly speculative. It necessarily involves consideration of a borrower's financial capacity under a variety of possible future economic scenarios. A court should be cautious in reaching a conclusion that there was no reasonable expectation in the absence of a detailed consideration of such scenarios and compelling evidence that there was no basis for the lender's expectations under any of such scenarios. In addition, a determination that a lender acting in good faith nevertheless had no reasonable basis for believing that its subsidiary had the financial capacity to generate cash flow sufficient to pay interest and repay principal over the term of the loan will inevitably rely heavily on the opinion of financial experts. Any expert opinion on such an issue, however, is at least as much a matter of judgment as it is of fact, except perhaps in exceptional circumstances. Accordingly, a court must have a very high degree of confidence in any such expert financial evidence before it finds that a lender acting in good faith nevertheless had no

reasonable basis for believing that its subsidiary had the financial capacity to generate cash flow sufficient to pay interest and repay principal over the term of the loan.

[191] Given the foregoing considerations, I conclude that, in order to find that the USS Debt Claims are "equity claims", the Court must be satisfied that either: (1) at the time of making an advance under the Term Loan or the Revolver Loan, USS did not believe that USSC would be able to repay such advance with interest out of USSC's cash flows over the term of the Term Loan or the Revolver Loan, as applicable; or (2) that, at the time of such advance, there was no reasonable basis on which USS could have expected USSC to generate cash flow sufficient to pay interest on, and repay the principal of, such advance over the term of the Term Loan and the Revolver Loan, as the case may be.

[192] Three related principles are also important for the analysis of the character of the USS Debt Claims.

[193] First, while the Term Loan and later the Revolver Loan constituted a significant part of USS' investment in USSC, the Loans do not represent all of that investment. As described above, USS has also made a significant investment that has been expressly treated as equity. This distinction is important. In this proceeding, the issue is limited to the characterization of the debt component of that investment. Clearly, the return on the equity portion of USS' investment will be dependent on the residual cash flow from USSC after payment of trade creditors as well as repayment with interest of the Term Loan and the Revolver Loan. However, the fact that these Loans form part of USS' total investment in USSC does not automatically mean that USS' expectation of repayment of these Loans is the same as its expectation of receiving a return on its equity investment.

[194] A parent corporation is able to divide its investment in an acquired corporation between debt and equity as it chooses. Such allocation of its investment is not determinative for the reasons discussed above. However, equally, such allocation must be respected unless it is demonstrated that the parent corporation did not have a reasonable expectation of repayment with interest of the portion of the investment which has been treated as debt when the loan was advanced. There is no basis in the CCAA for an automatic re-characterization into equity of a portion of an investment that has been structured as debt merely because the entire investment is, in a general sense, dependent for a return on the success of the investment. Put another way, a parent corporation can loan money to a wholly-owned subsidiary without that loan being treated automatically as part of the parent corporation's equity investment in the subsidiary.

[195] Second, the characterization of the USS Debt Claims must be analysed as of the date of the advances under each of the Term Loan and the Revolver Loan. Subsequent behaviour of either or both of the parties to the Term Loan Agreement or the Revolver Loan Agreement may be relevant, but only to the extent that such behaviour illuminates the intentions of the parties regarding the Term Loan or the Revolver Loan as of the date of the advances thereunder. Behaviour subsequent to any advance cannot, on its own, justify a re-characterization of such advance.

[196] Third, the characterization of the advances under each of the Term Loan and the Revolver Loan cannot be viewed in isolation from the economic circumstances in which the advances were made.

[197] In this respect, the economic backdrop to the advances under the Term Loan and the Revolver Loan during the period 2008 to 2013 can be summarized as follows. The advances under the Term Loan between October 31, 2007 and December 31, 2007 were made in the context of a buoyant steel market. Economic conditions changed dramatically in the autumn of 2008 after the collapse of Lehman Brothers and the onset of the financial crisis in that year. Worsening conditions prevailed throughout 2009 and into early 2010. Thereafter, in each of 2010, 2011 and 2012, USS and USSC experienced mini-cycles consisting of one or two encouraging quarters succeeded by a weak performance for the remainder of these years. In 2013, USS and USSC experienced a weak market throughout the year with the result that matters reached a critical stage. Under a new chief executive officer and a new chief financial officer, who assumed their offices effective September 1, 2013, USS commenced a review of its operations which revealed, among other difficulties, that while USSC represented 10% of USS' revenues, it contributed 50% of its operating losses.

General Considerations Regarding Determination of the Debt Re-characterization Issues

[198] Although the exercise of evaluation of the character of the Term Loan and the Revolver Loan ultimately requires a consideration of each of the advances individually, the issue is best addressed initially on a collective basis. As the Objecting Parties suggested, consideration of the characterization of the Term Loan and the Revolver Loan together recognizes, or perhaps more appropriately starts, from the position that the Term Loan and the Revolver Loan were used and administered by USS in the same manner and that the difference in their terms principally reflected tax and accounting considerations rather than any significant substantive difference in function. In this section, I propose to consider the probative value of the factors upon which the Objecting Parties principally rely as evidence that the Term Loan and the Revolver Loan were, in substance, equity contributions by USS to USSC.

[199] The Objecting Parties identified the following principal considerations or factors which, in their view, demonstrated that advances under the Term Loan and the Revolver Loan were equity contributions rather than loans for USSC: (1) the absence of any arm's length negotiation regarding the terms and conditions of the Loans; (2) the deferred interest payment dates and the long maturity dates of both the Term Loan and the Revolver Loan; (3) the history of interest payments and waivers under the Term Loan; (4) the absence of any security; (5) the extent of USS' control over the business, operations and financial performance of USSC; (6) the fact, as acknowledged by USS, that USSC would not have been able to obtain financing from a third-party bank or institutional lender in the amount and on the terms and conditions of either of the Term Loan or the Revolver Loan; and (7) their view that payments on account of the Term Loan and the Revolver Loan were effectively subordinated to payment of trade creditors.

[200] The Objecting Parties argue that, collectively, these considerations establish that USS had no expectation of repayment with interest of the advances under the Term Loan and the Revolver Loan out of cash flow from USSC. They say these factors demonstrate that, in substance, the Term Loan and the Revolver Loan were financial instruments under which USS was intended to receive the residual cash flow and assets of USSC as, and to the extent, available without an expectation of repayment with interest of either Loan, and were therefore capital contributions.

[201] Significantly, the Objecting Parties argue that each of the foregoing factors has probative value when measured against the standard of behavior that would be expected of a third-party lender. As mentioned above, this position reflects the approach in the Finnerty Report. USS argues that such a standard is inappropriate and, accordingly, that the factors upon which the Objecting Parties rely are not indicative of "equity interests".

[202] I propose to assess the submissions of the Objecting Parties respecting these general considerations in the following order. First, I will address in greater detail my understanding of the purposes and the administration of the Term Loan and the Revolver Loan. Then, I propose to address the issue of the significance of third-party lender behaviour in the context of a wholly-owned subsidiary relationship. Lastly, I will consider the probative value of the principal considerations relied upon by the Objecting Parties in light of the conclusions regarding the third-party lender standard.

The Purposes and Administration of the Term Loan and the Revolver Loan and the Differing Perspectives of the Parties

[203] As mentioned, USS established the Term Loan, and subsequently the Revolver Loan, with the intention that they would be the principal vehicles by which cash flows could be moved between USS and USSC and, in particular, surplus cash in USSC could be repatriated to USS. Additional equity injections were also made from time to time by USS, but only to the extent that USSC required additional capital to stay onside the "thin capitalization" rules under the *Income Tax Act* and for the purposes of the "de-leveraging" exercise described above.

[204] The initial advances of the Term Loan were directed to ABULC for the purpose of the Acquisition. Subsequent advances prior to and including December 31, 2007 were used by USS to repay the Credit Corp Loan, repay USSC's liabilities to SHC and, in a lesser amount, for working capital purposes. The advances in 2009 totaling $211.2 million were also used for working capital purposes. A substantial portion of the interest under the Term Loan in 2008 was paid in that year, two years before its due date. Such interest was paid out of surplus cash on hand as a result of the strong financial performance of USSC in 2008 prior to the slowdown that began in the fourth quarter of that year.

[205] USS then established the Revolver Loan in 2010 as a more tax-efficient means of moving cash between USS and USSC after withholding tax was eliminated on interest payments from USSC to USS, permitting tax-free interest payments from USSC to Credit Corp, which was an American corporation. For that reason, the Revolver Loan was denominated in U.S. dollars. Prior to the "de-leveraging" exercise in 2013, the outstanding balance under the Revolver Loan slightly exceeded the maximum availability of U.S. $500 million. In 2013, payments of principal and interest totaling approximately U.S. $390 million, that were funded out of equity injections aggregating over U.S. $680 million, reduced the outstanding balance to the amount of the First Tranche Indebtedness.

[206] In order to maximize its flexibility for such cash management purposes, USS structured both the Term Loan and the Revolver Loan to provide for the most generous maturity dates and interest payment dates possible given constraints imposed by tax legislation. Further, both the Term Loan Agreement and the Revolver Loan Agreement contained minimal representations and warranties and very basic events of default. In addition, until the Second Revolver Amendment,

both the Term Loan and the Revolver Loan were unsecured facilities. The Second Revolver Amendment in January 2013 provided for security on iron-ore pellets pursuant to the Security Agreement for the principal, if not the sole, purpose of maintaining the intended tax treatment for payments in respect of the Revolver Loan, given the interest waivers granted under the Term Loan in 2010, 2011 and 2012. As mentioned, with the arrival of a new chief financial officer effective as of September 1, 2013, USS began to evaluate its investment in USSC more closely. As of the end of October 2013, USS determined that it would only advance funds to USSC that it believed USSC would be able to repay. As a result, all subsequent advances were secured under the October Security Agreement and the November Security Agreement.

[207] There is, however, no suggestion that USS and USSC disregarded the debt character of the Term Loan and the Revolver Loan in moving cash between USSC and USS. Accordingly, all advances under the Term Loan and the Revolver Loan were documented as such and were distinguished, both in terms of documentation and accounting, from equity injections. All interest payments on the Loans were similarly documented by both parties and treated accordingly for tax and accounting purposes. Principal payments were similarly documented by both parties. There is no evidence that the payments made in respect of the Term Loan or the Revolver Loan failed to satisfy the requirements under Canadian and American tax legislation for treatment as debt and, in particular, that any payments were deemed to be dividends.

[208] On the other hand, there is no doubt that the Term Loan and the Revolver Loan were provided by USS to USSC on terms and conditions that USSC could not have obtained from third party banks and other non-bank institutional providers of term financing and operating credit facilities. In particular, the payment provisions respecting interest and principal, and the absence of security, would not have been available to USSC.

[209] USS says that both the documentation and the manner of administration of the Loans reflect debt obligations. USS says that there is nothing in the cash management arrangements described above between a parent and a wholly-owned subsidiary that can justify re-characterization of the Loans as capital contributions for the purposes of the CCAA. In particular, USS argues that nothing in these financing arrangements suggests that it did not expect to receive repayment with interest of the funds advanced under the Loans. It also says that the fact that the Term Loan and the Revolver Loan were provided to USSC on terms that were not available to USSC from third parties is irrelevant.

[210] The Objecting Parties argue that USS established and administered the Term Loan and the Revolver Loan in the manner of, and using its rights as, a shareholder rather than a lender. They say that USS' actions are collectively more consistent with an intention to receive the residual cash flow and assets of USSC, as and when available, without any expectation of repayment with interest of the advances under the Loans. A more precise expression of their position is that the Term Loan Agreement and the Revolving Loan Agreement reflect arrangements under which USS intended at all times to return excess cash to USS when available and to write off the principal or interest in respect of the Loans to the extent that payments were due and sufficient cash was not available. I have excerpted below certain passages from the written submissions of the Union and the Province that I think capture the essential approach of these parties and which also assist in clarifying the positions of these parties.

The Relevance of the Third-Party Lender Standard

[211] Clearly, a significant fact in this proceeding is that, at all relevant times, ABULC and USSC, as applicable, were wholly-owned subsidiaries of USS. In addition, unlike many parent-subsidiary relationships in which the subsidiary carries on a business independently of the parent, USSC was very closely integrated into the business of USS. After the Acquisition, all management and operational functions previously conducted by Stelco were effectively centralized within USS. USSC became a part of the North American flat-rolled steel division of USS. This relationship is significant in two related respects.

[212] The Objecting Parties argue that the USS control of USSC is an important factor in assessing whether, in substance, the Term Loan and the Revolver Loan were debt instruments or contributions to capital. They say that USS had a significant ability to influence the profitability of USSC through such control. They say that such control is, in some way, an indication of an equity contribution. I will address this below in the next section.

[213] The issue of control is also significant for present purposes as a gateway to the related issue of the relevance of a third-party lender standard as a basis for evaluation of the terms and conditions, as well as the administration, of the Term Loan and the Revolver Loan. As mentioned, USS provided financing to USSC that would not have been available to USSC from banks and other institutional lenders. The Objecting Parties place great weight on this factor as demonstrating that the Term Loan and the Revolver Loan were not real loan transactions, but rather were disguised equity contributions. Equally important, most, if not all, of the *AutoStyle* factors identified above upon which the Objecting Parties rely are informed, in whole, or in part, by a comparison of USS' actions against a standard of a typical third-party lender.

[214] The Objecting Parties suggest the Court should look to a third-party lender standard in two principal respects – in order to assess the terms and conditions of the Term Loan and the Revolver Loan and in order to assess the actions of USS and USSC in the administration of these Loans including payments thereunder. As these are significant factors in the analysis proposed by the Objecting Parties, I propose to address these two issues in some detail.

[215] It is important to recognize at the outset that there is no necessary reason why a parent corporation would act in the same manner as a third-party lender in the provision of financing facilities to its wholly-owned subsidiary. In particular, the terms and conditions of lending arrangements between a wholly-owned subsidiary and its parent will, in many if not most cases, depart from typical lending arrangements between a third-party lender and a borrower.

[216] As a practical matter, compliance with tax regulations in order to ensure favourable tax treatment will be a significant, if not the main, driver regarding these matters. In this case, USS determined the relative amounts of loans and equity injections based principally on tax considerations to the USS group of companies considered as a whole. Generally, these considerations dictated maximization of debt to obtain interest deductibility under the United States *Internal Revenue Code*, 26 U.S.C., subject to compliance with the "thin capitalization" rules under the *Income Tax Act*, which established a maximum debt/equity structure.

[217] In addition, in a wholly-owned subsidiary relationship, there is no need for extensive documentation, nor is there a need for the types of contractual protections typically found in

commercial loan agreements. Given the parent's ability to control the subsidiary's actions as its sole shareholder, there is also no need for a strict schedule of repayment of principal. Further, there is no reason why a parent corporation would enforce any rights of default that may arise in the course of a loan so long as the parent corporation believes that the subsidiary has value. Such rights are asserted only as required to protect the parent corporation in the event that a third party asserts its rights as a creditor against the subsidiary or to terminate the parent corporation's support of the subsidiary. Similarly, it is not realistic to expect that a wholly-owned subsidiary will conduct its affairs pursuant to a corporate governance structure that includes independent directors until such time as the interests of the parent corporation and the subsidiary diverge.

[218] There is nothing improper in any of the foregoing arrangements. To be clear, the Objecting Parties do not suggest that there is. They submit that a parent corporation can choose to structure its arrangements however it chooses for tax and other purposes. However, they say that such arrangements should not govern the determination of whether such loans give rise to "equity claims" for the purposes of the CCAA. On their approach, the determination of the treatment of such claims under the CCAA should be made on the basis of a different test than that which satisfied tax and other regulatory rules and regulations prior to an insolvency.

[219] The dispute between the parties, and a principal issue on this motion, is therefore whether there are any consequences, in the context of CCAA proceedings, to a parent corporation that has structured its investment in a wholly-owned subsidiary in the manner of the Loans, that is, in a manner that complies with all applicable tax and other regulations but is not consistent with how a third-party lender would have structured any loan facilities in favour of USSC and how any such lender would have acted in the circumstances of USSC's subsequent financial performance.

[220] A comparison of the relationship between USS and USSC against a notional relationship between USSC and a third-party lender provides a helpful clarification of certain factors that are relevant for present purposes, as is discussed below. However, I find that a comparison between the behavior of USS and the behavior of a notional third-party lender is not an appropriate test in the evaluation of whether the advances under the Term Loan and the Revolver Loan were capital contributions to USSC. I reach this conclusion for the following reasons.

[221] First, the Loans were structured, and excess cash was moved between USSC and USS, in the manner described above for legitimate business reasons and in accordance with all applicable legal requirements. There is no express authority in the CCAA for disregarding these arrangements in such an evaluation apart from the very general language in the definition of "equity claim" referring to a return of capital. In particular, there is no express authority for disregarding the business purpose of financing arrangements in the evaluation of whether loan instruments are, in substance, "equity interests" giving rise to "equity claims".

[222] Second, the Objecting Parties assert that the USS Debt Claims constitute claims for a return of capital. In the absence of any statutory definition of capital, or guidance regarding the determination of capital, for the purposes of the definition of an "equity claim", considerable weight should be given to the accounting and tax determination of capital of the debtor company in any CCAA proceedings. In this case, there is no suggestion that the Term Loan or the Revolver Loan were treated as capital for such purposes.

[223] Third, the Objecting Parties submit, as an operating principle, that the less the Term Loan and the Revolver Loan resembled financing available from a third-party lender, and the less the actions of USS in the administration of the Loans resembled those that would have been expected of a third-party lender, the more the advances under the Loans resemble equity contributions. I do not accept this principle for the reason that I do not see a necessary connection between a failure to adhere to the third-party lender standard and an absence of an expectation of repayment with interest of a loan in the circumstances where the departure from the third-party lender standard reflects a valid business purpose.

[224] I accept that there may be circumstances where the departure from a third-party lender standard may not serve any valid business purpose related to a parent-subsidiary relationship. In such circumstances, it may well be that such actions would suggest an equity contribution, that is, that the only explanation for the parent corporation's actions is that the loan transaction was in fact a capital contribution. However, that is not the case in the present circumstances. As mentioned above, the interest payment terms, the maturity dates of the Loans and the absence of a schedule for principal repayments provided USS and USSC with a certain amount of flexibility to align the payment of interest and the repayment of principal with the economic performance of USSC against the backdrop of a highly cyclical industry. In particular, it provided USSC with the ability to defer payments of interest and principal for a period of time in the event of adverse economic performance without triggering default provisions or a reversal of income expense for tax purposes.

[225] Fourth, as a related matter, the third-party lender standard ignores the very real business purposes that a parent corporation could have for departing from a third-party lender standard in the administration of financing established in favour of a wholly-owned subsidiary.

[226] The Objecting Parties submit that the less a parent corporation acts to enforce its rights in an insolvent situation in the manner that would be expected of a third-party lender, the more it demonstrates that the financing arrangements between the parent corporation and the subsidiary are in fact equity contributions rather than loans. This submission ignores the reality that a parent corporation which believes that there is value remaining in a subsidiary, even if the subsidiary is technically insolvent, will not act to enforce its security in the manner that would be expected of a third-party lender whose objective is necessarily limited to maximizing the prospects for the immediate recovery of its principal and interest. Nor would a parent corporation seek to negotiate some further benefit such as fees or additional equity in such circumstances. The subsidiary has no additional benefit to give when the parent already owns 100% of the benefit of its enterprise. Given such considerations, the actions of a parent corporation in departing from a third-party lender standard do not evidence the absence of an expectation of repayment with interest of a loan to its subsidiary when the loan was made. Moreover, in this respect, the position of the Objecting Parties contradicts the purposes of the CCAA, which should encourage efforts that seek to continue the operations of a distressed subsidiary.

[227] Fifth, more generally, the premise underlying the position of the Objecting Parties, as is demonstrated by the foregoing discussion, is that a parent corporation is acting as a shareholder to the extent that it fails to act in a manner that would be expected of a third-party lender. They express this argument by saying that, to the extent a parent corporation is not looking at a loan to its subsidiary through the lens of a third-party lender, it must be looking at the loan from the

perspective of a shareholder and, as such, in reality, the loan must be equity. In short, a parent corporation cannot wear two hats at the same time.

[228] I do not think this is correct. A parent corporation lending to its wholly-owned subsidiary can have regard to the existence of its rights as a shareholder in structuring and administering a loan to its subsidiary without ceasing to be a lender. The issue to be considered is whether the actions of the parent corporation demonstrate that it had no expectation of repayment with interest of the loan. There is no necessary connection between a parent corporation lending to a subsidiary on a basis that departs from a third-party lender standard and the absence of such an expectation.

[229] Sixth, there is also a significant issue with the definition of a third-party lender proposed as the standard by the Objecting Parties. The Objecting Parties propose the standard of a bank or an institutional lender providing unsecured term or operating facilities on the basis of their expert financial evidence regarding an appropriate proxy for the Term Loan and the Revolver Loan. This is an unduly restrictive standard given the purpose of the test for an "equity claim", which is to assist in determining whether USS had a reasonable expectation of repayment with interest at the time it extended advances under the Term Loan and the Revolver Loans. While the willingness of a third-party to lend on the terms provided by a parent corporation could support such a conclusion, the absence of third-party lender financing is not sufficient to establish that no other financing would have been available to the subsidiary on a viable basis. Where a party seeks to disprove the alleged reasonableness of an expectation of repayment of a loan with interest, or the absence of any debt capacity of a borrower, it is necessary to canvas the availability of viable financing across capital markets more broadly.

[230] Lastly, the Objecting Parties acknowledge that the standard that they propose would apply solely for purposes of proceedings under the CCAA and, perhaps, the BIA. There are three difficulties with this result.

[231] First, as mentioned, a court should give considerable weight to the characterization of payments to the extent that third parties, such as the Canadian and American tax authorities, have accepted the treatment of such payments in the past in the absence of any express authority in the CCAA to do otherwise. In this case, there is a history of characterization of payments consistent with loan transactions that includes not only the loan documentation but also interest payments, principal repayments and interest waivers under the Term Loan. There is no evidence that either the Canadian or the American tax authorities have raised any issue with the treatment of any such payments for tax purposes.

[232] Second, while tax treatment cannot be determinative, these tax regimes represent another third-party standard that has some independent validity in evaluating the substantive reality of loan instruments.

[233] Third, as a policy matter, I see no policy benefit in having separate rules in the tax and accounting domain, on the one hand, and in the CCAA domain on the other. It is important for stakeholders in a corporation to have rules that yield reasonable certainty for planning purposes. A consequence of the approach proposed by the Objecting Parties would be that a parent corporation seeking such certainty in respect of the treatment of a loan to its subsidiary would have to limit its financing arrangements to those which an independent consultant considers to be

comparable to financing facilities that would be provided by a notional third-party lender. There are a number of difficulties with this approach from a policy perspective for which there is no obvious corresponding benefit. The principal difficulty is the overriding of valid business purposes by the imposition of a restrictive standard for the purposes of any future CCAA proceedings. In addition, there would be additional costs associated with such a policy, a need for updates as advances are made over time in changing market conditions, and a potentially inefficient limitation of financing options from a financial perspective.

[234] Based on the foregoing considerations, I am not persuaded that the third-party lender standard proposed by the Objecting Parties, and which underlies many of the specific factors upon which the Objecting Parties rely, is appropriate in the present context for determining whether the Loans were, in substance, capital contributions. This conclusion has the following implications in respect of the manner in which the factors identified above are to be applied in the evaluation of the Term Loan and the Revolver Loan as debt obligations or capital contributions.

[235] First, with respect to factors (1) to (4), such factors are relevant to the issue of the expectations of USS at the time of advances under the Loans. However, these considerations must be evaluated in terms of what they indicate about the expectations of USS without regard to any comparison with any notional third-party lender. In other words, it is not a relevant consideration in determining whether USS had an expectation of repayment with interest that a notional third-party lender would not have provided financing arrangements to USSC having these features.

[236] Second, the fact that a notional third-party lender would not have extended financing facilities to USSC on the terms and conditions of the Term Loan and the Revolver Loan is also not determinative of whether USSC had the debt capacity to service the advances under the Term Loan and under the Revolver Loan when they were made. It is therefore not determinative of the reasonableness of USS' expectation of repayment with interest of the Loan.

[237] The foregoing conclusion does not, however, foreclose entirely the relevance of the availability of financing from independent sources. As discussed above, I accept that a test based on the availability of financing from an external source of financing, not limited to a third-party lender, could be a means of evaluating the debt capacity of a wholly-owned subsidiary. Framed in such terms, such a test would bear on the reasonableness of a parent corporation's expectations of repayment of the principal with interest of a particular loan or advance based on the debt-capacity of the subsidiary. However, there is no reason to narrow consideration of such debt capacity to the availability of third-party lender financing, unless the evidence clearly establishes that no other financing facilities would have been available to the subsidiary had it sought external financing.

[238] Third, in the analysis below, I do not accord any significant weight to the test suggested by the Objecting Parties – that the less the Term Loan and the Revolver Loan reflect the characteristics of a third party loan from a bank or other institutional lender, the more such Loans resemble equity. In my opinion, to the extent that such Loans depart from the third-party lender standard for reasons that have a legitimate business purpose that is related to the wholly-owned subsidiary relationship or its business, the Court cannot disregard the legitimacy of such arrangements in its analysis. Given a legitimate business purpose for departing from the

standard of behavior of a third-party lender, there is no necessary reason why a parent corporation could not also have had an expectation of repayment with interest of any loan advance at the time of such advance notwithstanding that it did not act in the same manner as a third-party lender. As discussed above, there is no necessary reason why a parent corporation cannot be both a lender and a shareholder even if, as a lender, it does not conform in all respects to the standard of a third-party lender.

Analysis of the Principal Considerations Relied Upon by the Objecting Parties

[239] I turn then to a consideration of the probative value of the general factors relied upon by the Objecting Parties in the analyses below of the Term Loan and the Revolver Loan. As set out above, the Objecting Parties say that the Term Loan Agreement and the Revolver Loan Agreement reflect arrangements under which USS intended at all times to return excess cash to USS when available and to write off the principal or interest in respect of the Loans to the extent that payments of either were due and sufficient cash was not available.

[240] In this section, I will address, in order, the extent to which the seven principal factors relied upon by the Objecting Parties are of assistance in the analysis of the Term Loan and the Revolver Loan in light of the conclusions reached above. The seven principal factors are the following: (1) the absence of any arm's length negotiation regarding the terms and conditions of the Term Loan or the Revolver Loan; (2) the deferred interest payment dates and the long maturity dates of both the Term Loan and the Revolver Loan; (3) the history of interest payments and waivers under the Term Loan; (4) the absence of any security; (5) the extent of USS' control over the business operations and financial performance of USSC; (6) the fact, as acknowledged by USS, that USSC would not have been able to obtain financing from a third-party bank or institutional lender in the amount and on the terms and conditions of either the Term Loan or the Revolver Loan; and (7) the view of the Objecting Parties that payments on account of the Term Loan and the Revolver Loan were effectively subordinated to payment of trade creditors.

[241] First, the Objecting Parties suggest that the lack of any negotiation between USS and ABULC regarding the Term Loan, and the absence of any substantive negotiations between USS and USSC regarding the Revolver Loan, suggest that the advances under the Loans were in the nature of equity injections rather than *bona fide* debt. I do not consider these circumstances to be of any value in addressing the issues on this motion. The limited negotiations between these parties is a reflection of the wholly-owned subsidiary relationship that is the starting point for such issues, but it is a neutral fact that does not bear in any way on the reasonableness of the expectations of USS regarding repayment with interest of the advances under the Term Loan and the Revolver Loan.

[242] Second, the Objecting Parties submit that the two-year interest payment provision in the Term Loan and the Revolver Loan, and the lengthy maturity dates for the Loans, suggest these arrangements were capital contributions. However, the terms and conditions of the Term Loan and the Revolver Loan make express provision for the payment of interest on fixed dates and the repayment of principal by a fixed maturity date. While these terms were acknowledged to be generous, the fact remains that each Loan fixed the maximum amount payable thereunder as interest and principal and provided fixed dates for the payment of accruing interest and the repayment of the principal amount of the Loans. In particular, the interest payment dates were time-limited. Setting aside any comparison with the terms expected in third-party lender

arrangements for the reasons set out above, there is nothing in the terms of the Loans, on their own, that would support an inference that USS did not expect to receive repayment with interest of all advances made under the Loans. In particular, the existence of a long maturity date and the absence of a schedule of repayments is not a basis for inferring that USS did not expect USSC to repay the Term Loan. The Term Loan did not prevent earlier repayment of principal. In addition, USS was in a position to require USSC to repay principal without a contractual schedule of repayments.

[243] Accordingly, on their face, neither the Term Loan nor the Revolver Loan is more consistent with receipt of the residual cash flow and assets of USSC as the Objecting Parties suggest. Any such inference must be based on the actions of USS and USSC in the administration of the Loans.

[244] Third, accordingly, the Objecting Parties argue that the Court should infer from the manner in which interest payments were treated under the Term Loan that the Loans were intended to be capital contributions rather than debt, i.e., that there was never any expectation of repayment with interest of the Loans. There are two aspects of the interest payment history in respect of the Term Loan that will be addressed separately – the accelerated payment of interest in 2008 and the interest waivers commencing in 2010.

[245] The Objecting Parties argue that the acceleration of the interest payments under the Term Loan in 2008 evidences an intention to treat the Term Loan as a capital contribution. In making this argument, the Objecting Parties rely on the testimony of Dr. Finnerty who suggested that the payment of interest under the Term Loan in 2008 ahead of the due date in 2010 exhibited behavior that was more characteristic of the payment of dividends rather than interest.

[246] I accept that it is possible that the payment of interest could resemble a dividend in circumstances in which there is no reasonable explanation for the timing or amount of payments made outside the provisions of a loan agreement, for example, a payment in excess of accrued interest by way of an alleged pre-payment of interest. However, where the timing of interest payments is consistent with a legitimate business purpose and in accordance with the provisions of a loan agreement, the Court cannot disregard such circumstances in assessing the expectations of the parent corporation regarding the loan.

[247] In this case, the Term Loan permitted, but did not require, a deferral of interest payments for a period of time. The argument based on Dr. Finnerty's evidence proceeds on the unrealistic premise that, given such a provision in a loan agreement, a subsidiary would not pay interest to its parent corporation until the end of the permitted interest deferral period even if an earlier payment would be more efficient financially. In other words, the argument relies on a third-party lender standard which is rejected for the reasons discussed above. More generally, where there is a legitimate business reason for the flexibility provided in the loan agreement, I do not see any necessary connection between the availment of that flexibility and either the characterization of the payment as a dividend or the expectation of the parent corporation regarding repayment of the loan with interest.

[248] In the present circumstances, the accelerated interest payments reflected very favourable financial results of USSC during the first three quarters of 2008. There was no legitimate reason for USSC to defer payment of interest, which was compounding while outstanding, to the

interest payment date if it had cash available for such purpose. The Term Loan Agreement permitted a deferral of interest payments for a period of time to accommodate an adverse financial performance from time to time. However, it did not require such a deferral in the event of a favourable economic performance. The presence of this provision does not evidence an intention of USS and USSC that USSC would hold on to excess cash at its own cost in such circumstances.

[249] Accordingly, I am not persuaded that the acceleration of interest payments in 2008 is indicative of an intention on the part of USS to treat the Term Loan as a capital contribution rather than as a debt obligation.

[250] The Objecting Parties also argue that the interest payment waivers granted in favour of USSC commencing in 2010 evidence the absence of any expectation of repayment with interest of the Term Loan. Insofar as the Objecting Parties urge the Court to draw such an inference from the existence of the interest waivers without having regard to a third-party lender standard, this issue is addressed later in these Reasons.

[251] I note, however, that Dr. Finnerty's opinion was based on a somewhat different approach. He suggested that, from the perspective of financial economics, USS' actions in respect of the interest waivers reflected the behavior of a shareholder rather than a lender. The position of Dr. Finnerty and the Objecting Parties is that, in the circumstances of non-payment of interest, third-party lenders will obtain some value in negotiations with borrowers as a condition of granting such waivers. As evidence of an equity interest, they point to the absence of any enforcement proceedings on the part of USS to protect its interest as a lender, and of any negotiations to obtain a *quid pro quo* for, in particular, the grant of such waivers of interest.

[252] Given the finding above regarding the appropriateness of the third-party lender standard, the Court does not draw any inference from the absence of any enforcement proceedings or other actions on the part of USS in respect of the interest waivers. In this case, the application of such a standard also reflects an unrealistic premise upon which the argument for equity treatment is based. As mentioned above, in wholly-owned situations, enforcement proceedings are counter-productive so long as the parent corporation believes the subsidiary still has value. It is also axiomatic that the subsidiary cannot give the parent any additional value as a *quid pro quo* for obtaining a waiver of its interest obligations since the parent already owns all of the subsidiary's equity value. The probative value of the interest waivers is discussed further below.

[253] Fourth, the Objecting Parties submit that the absence of security for the Term Loan or the First Tranche Indebtedness is probative of the expectations of USS at the time it extended advances under the Loans. This argument also relies implicitly on a comparison with a third-party lender standard. If such a comparison is disregarded, I conclude that the absence of security is not indicative of a capital contribution for the following reasons.

[254] As discussed above, and as the history of the Revolver Loan demonstrates, as the sole shareholder of USSC, USS had no need to require security for its loans to USSC until it became concerned about the ability of USSC to repay any funds advanced to it. As such, the fact that USS required security for advances made after October 2013 is more significant as evidence of the expectations of USS in October 2013 than the absence of any security for advances made

prior to that date. In short, the Objecting Parties have not demonstrated a necessary connection between an absence of security for the Term Loan or the First Tranche Indebtedness and an absence of any expectation of repayment with interest of the Term Loan or the First Tranche Indebtedness.

[255] Moreover, the implication of the position of the Objecting Parties is that, to protect itself in possible insolvency proceedings, a sole shareholder must lend on an asset-backed basis, i.e., take security on the assets of the enterprise, to avoid characterization of its loan as equity. This cannot have been the intention of the definition of "equity claims" under the CCAA insofar as such an implication would, among other things, encourage a parent corporation to take a priority over claims of trade creditors and thereby make a restructuring of an enterprise in an insolvency situation more difficult.

[256] Fifth, for the following reasons, I am not persuaded that the extent of USS' control of USSC is a factor to be taken into account in assessing whether the Term Loan and the Revolver Loan were, in substance, equity contributions by USS.

[257] As a polar case, I accept that there may be circumstances in which a parent corporation's expectation from the outset is that it will sacrifice a subsidiary's profitability over the long-term for the benefit of the consolidated enterprise. In such circumstances, a court could find that the parent corporation had no intention of causing the subsidiary to repay with interest any financing extended to the subsidiary or, more precisely, no expectation that the subsidiary would generate sufficient cash flow to enable it to make such payments based on the parent's anticipated business plan for it. In such circumstances, a court could also find that the entire amount of the financing extended by the parent corporation to the subsidiary was, in reality, an equity contribution.

[258] However, the Objecting Parties have expressly advised the Court that they do not take that position in this proceeding. In any event, the evidence is not sufficient to justify such a conclusion in the present circumstances. In particular, among other considerations, the history of the Term Loan and the Revolver Loan is too short, and the impact on the entire USS business of the recessionary environment after late 2008 was too significant, to enable the Court to draw such a conclusion.

[259] This leaves the question of whether control of a wholly-owned subsidiary that does not go so far as to render the profitability of the subsidiary a matter entirely in the sole discretion of the parent corporation can constitute a consideration to be taken into account in the analysis of whether loans made by the parent corporation are debt or are, instead, equity contributions. I accept that such control requires a court to take a "good hard look" at the substantive reality of any such loans, in this case being the advances under the Term Loan and the Revolver Loan. Beyond that, however, in this case, I think that USS' control is the point of departure, rather than an independent factor, for the following reasons.

[260] First, and foremost, as mentioned, there is no overriding authority in the CCAA to disregard entirely the manner in which parties, including related parties, have structured their affairs. As set out above, I think a court must give effect to such structure unless and until, in the case of a loan from a parent corporation to a subsidiary, there is other evidence establishing that the parent did not reasonably expect to receive repayment of the loan with interest at the time of

the making of the loan. In other words, the existence of control is not a basis for such an inference on its own.

[261] Second, the submission of the Objecting Parties that USS' control is an independent factor demonstrating an equity contribution proceeds on the basis of a distinction between a lender's rights and a shareholder's rights that is untenable in the present circumstances. The Objecting Parties argue, in effect, that USS acted in its capacity as a shareholder, rather than as a lender, in causing USSC to repay monies to it and, therefore, such payments should be treated as dividends.

[262] This argument is based on a false dichotomy. No lender has a right to compel the repayment of principal or the payment of interest. The lender's rights are restricted to enforcement in the event of non-payment. The debtor alone decides whether to pay principal or interest. The implication of this argument is that a parent corporation must renounce its rights as a shareholder to cause payments under a loan agreement. This is not only unrealistic but also counter to the conclusion that a parent corporation can have regard to its rights as a shareholder while acting as a lender. Accordingly, the fact that USS instructed USSC with respect to the payments to be made cannot on that account result in a characterization of such payments as dividends, or of the Loans as capital contributions.

[263] Sixth, for the reasons set out above, I conclude that the fact that USSC could not have obtained financing from a third-party lender on the terms and in the amounts of the Loans is not an independent factor that assists in evaluating USS' expectations regarding repayment with interest of the advances under these Loans at the time that they were made.

[264] Seventh, the remaining consideration is the view of the Objecting Parties that USS effectively subordinated its position to the other creditors of USS by paying interest on the Term Loan and the Revolver Loan only after such other creditors were satisfied on an on-going basis. In doing so, the Objecting Parties say USS acted like a shareholder rather than a lender, thereby evidencing the absence of any expectation of repayment with interest of the Loans.

[265] As a factual matter, it is correct that USSC paid interest on the Term Loan and the Revolver Loan only after its arm's length creditors were satisfied on an on-going basis. From 2007 until shortly prior to the Filing Date, USS funded USSC with debt or equity in order to permit USSC to pay its trade creditors on an ongoing basis. Moreover, as mentioned, USS waived a significant amount of interest that accrued and became due under the Term Loan and made no interest payments on the remaining accrued interest.

[266] This raises the question of whether such evidence demonstrates that USS intended that the Term Loan and the Revolver Loan would be subordinated to payment of USSC's other obligations and, if so, whether such arrangements demonstrate that USS did not expect to receive repayment with interest of the Loans. There are a number of issues bound up in this argument that need to be separated.

[267] First, it is important to note that there is no suggestion that USS intended a legal subordination of its claims in respect of either the Term Loan or the Revolver Loan to claims of third party creditors of USSC. Indeed, after October 2013, all fresh advances under the Revolver Loan were secured and, therefore, ranked ahead of the trade creditors of USSC.

[268] Second, in any event, subordinated debt is not synonymous with a capital contribution. For present purposes, subordinated debt remains debt, subject to demonstration that a borrower could not have obtained subordinated debt on any basis from external sources, that is, did not have the debt capacity to obtain external financing in the amount of the Term Loan or the amount of the First Tranche Indebtedness. In such event, such evidence would cast serious doubt on a parent corporation's expectation with respect to repayment with interest of the alleged subordinated debt. As discussed below, however, there is no such evidence in the present case.

[269] Third, I am not persuaded that the actions of USS and USSC described above are properly characterized as subordination for present purposes. In the face of a significantly changed economic and financial environment described above, USS chose to defer rather than subordinate the repayment of the principal of the Loans and the payment of interest, except to the extent of the waived interest. However, USS left its options open regarding the treatment of amounts outstanding under the Term Loan in the future.

[270] Fourth, and most important, there is no evidentiary connection between the factual circumstances which the Objecting Parties describe as effective subordination of the Term Loan and the Revolver Loan and the expectation of USS regarding repayment with interest of the Loans at the time the advances were made thereunder. As described elsewhere in these Reasons, the economic circumstances commencing in 2008 established a reason for the actions that USS and USSC took subsequently which the Objecting Parties say constituted effective subordination of the Loans. There is, however, no evidence of an intention to implement such actions or, more generally, to implement a principle of effective subordination, at the time of the advances under the Loans.

[271] Accordingly, I am not persuaded that the argument of alleged effective subordination of the Term Loan and the Revolver Loan supports the position of the Objecting Parties that USS did not expect to receive repayment with interest of advances under the Term Loan or the Revolver Loan.

Analysis and Conclusions Regarding the Re-characterization Claim in Respect of the Term Loan

[272] I propose to set out my analysis of the debt re-characterization claim of the Objecting Parties with respect to the Term Loan after first setting out the position of the Objecting Parties in their written submissions. I would note that, at the trial, the Objecting Parties concentrated on a subset of these considerations which are addressed in these Reasons.

Positions of the Parties

The Union

[273] The essence of the position of the Union with respect to both the Term Loan and the Revolver Loan is captured by the two paragraphs below which are taken from the supplementary written submissions of the Union:

> Critically, USS always expected and intended that USSC's repayment of amounts owing under both the Term Loan and the Revolver Loan was contingent on USSC's performance.

> The evidence is clear that USS only expected to receive payments on account of interest and principal if and when USSC was able to make them, and not in accordance with the terms of the agreements. On discovery, Mr. Brockway's evidence was that USS "anticipated that the ability to repay that portion of the debt would be dependent on the success of Stelco's business going forward."

[274] The Objecting Parties do not merely assert that USS expected to disregard the timing requirements of the Term Loan Agreement and the Revolver Loan Agreement with respect to the movement of available cash from USSC to USS. Rather, they say that, from the outset of each of the Term Loan and the Revolver Loan, USS did not expect USSC to be able to repay the advances under such Loans, and the interest on such advances, and therefore expected to write off a significant portion of such obligations as they fell due.

[275] In its factum, the Union argues that the Term Loan should be re-characterized as equity based principally on the following seven *AutoStyle* factors: (1) the ability of USSC to obtain similar financing from outside lending institutions; (2) the source of repayments of the Term Loan; (3) the presence or absence of a fixed maturity date and schedule of payments; (4) the absence of security for advances under the Term Loan; (5) the absence of a sinking fund to provide for repayments; (6) the extent to which the advances under the Term Loan were effectively subordinated to the claims of outside creditors; and (7) the inadequacy of capitalization of ABULC at the date of the initial advance under the Term Loan.

[276] The Union also says that the lack of negotiation between USS and USSC regarding the Term Loan and the fact that the principal purpose of the initial advances under the Term Loan was the acquisition by USS of capital assets also support a finding of a contribution to capital rather than debt.

The Province

[277] The general approach of the Province with respect to both the Term Loan and the Revolver Loan is set out in the following excerpts from its factum:

> The context of the Term Loan is crucial for the characterization exercise. … Essentially, USSC operated as a division of the USS organization. This same context also applies to the Revolver….
>
> USS' attitude to the financing of USSC reflected what its attitude would be in funding one of its operating divisions – the money went where and when needed. There was no consideration or expectation that the funds would be treated other than equity – the investment would yield returns if, and only if, the business prospered. Advances were motivated by whether the global business would benefit from the allocation of resources to the facility, and not based upon any analysis of the profitability or credit-worthiness of the business unit….
>
> USS' loose approach to interest from USSC is understandable in the context of the complete control of USSC by USS discussed above. Whether USSC had the wherewithal at any point in time to pay interest was utterly dependent on the production USS assigned to it, the intercompany allocation of raw materials (and

> their cost) and USSC's personnel – all controlled by USS. Presumably, USS believed sending the money to USSC on a non-interest bearing basis allowed USS to earn a better return elsewhere in the global business.

[278] In its factum, the Province argues that the Term Loan should be re-characterized as equity based principally on the following three allegations: (i) there was no expectation that USSC would pay interest on the Term Loan advances; (ii) there was no expectation that USSC would repay the principal of the Term Loan advances; and (iii) the Term Loan was not provided by, nor available from, a third-party lender on commercial terms. I note that the first two considerations are not actually referred to in *AutoStyle*, although, as discussed above, I think that they are fundamental issues in respect of the re-characterization issue.

[279] The Province also suggested that the following four attributes of the Term Loan, which reflect factors referred to in *AutoStyle* and are included in the considerations upon which the Union relies, also demonstrate that it is, in substance, equity rather than debt: (1) the initial advances under the Term Loan were used to acquire a capital asset, being the outstanding shares of Stelco; (2) ABULC's capital structure was thinly or inadequately capitalised at the date of the Acquisition when the initial advances were made under the Term Loan, especially in light of Stelco's historical operating performance; (3) the failure to provide for security for the Term Loan; and (4) the failure to establish a sinking fund for repayment, particularly in view of the 30-year term of the Term Loan.

USS

[280] USS submits that a number of the *AutoStyle* factors considered by American courts refute, rather than support, the Objecting Parties' re-characterization argument, including: (1) the documents entered into between USS and USSC regarding the Term Loan on their face purport to evidence indebtedness and are titled "Loan Agreements"; (2) the parties intended to enter into a loan transaction; (3) the Term Loan has a fixed maturity date; (4) the Term Loan provides for a specified applicable interest rate; (5) under the Term Loan, USS has the right to enforce payment of interest and principal; (6) USS did not acquire any management control rights in exchange for the funds advanced under the Term Loan; (7) USS did not subordinate any amounts owing under the Term Loan to USSC's other creditors as a matter of law; and (8) a substantial portion of the funds advanced under the Term Loan were used to finance USSC's ongoing operations. In addition, USS relies on statements in a recent American decision, *In re Alternate Fuels Inc*., 789 F.3d 1139 (10th Cir. 2015), to the effect that the identity of interest between USS and USSC and any undercapitalization of ABULC should not be material considerations in the context of a loan from a parent to a wholly-owned subsidiary.

Analysis and Conclusions

[281] As set out above, the claim of the Objecting Parties that the Term Loan should be characterized as an "equity claim" requires addressing two matters: (1) the expectation of USS regarding repayment of principal and interest on the Term Loan out of cash flows of USSC over the term of the Term Loan; and (2) the reasonableness of such expectations. I note that, while these are discrete issues, the evidence referred to below that is relevant to the expectation of USS at the time of any particular advance can also be relevant to the reasonableness of such expectation.

[282] As described above, most of the Term Loan advances were advanced to ABULC between October 31, 2007 and December 31, 2007. However, further advances in the aggregate principal amount of $211.2 million were made in 2009. It is therefore necessary to address the characterization of the Term Loan advances in these two periods of time separately. In each case, I will address the application of the general considerations discussed above to the USS expectation regarding repayment of the Term Loan with interest and will then consider certain additional arguments of the Objecting Parties specific to the Term Loan that have not already been addressed above.

Term Loan Advances at the Time of the Acquisition

[283] The advances made to USSC in respect of the Acquisition between October 31, 2007 and December 31, 2007 have been set out above. USS says that it expected to be repaid the principal of the Term Loan outstanding at December 31, 2007 with interest over the course of the Loan, even if it could not anticipate the timing of such payments given the cyclical nature of the steel industry.

[284] USS relies principally on the evidence of Brockway with respect to the facts pertaining to its expectations at the time of the Acquisition and the initial advances under the Term Loan. Brockway testified that USS based its decision to acquire Stelco on a financial model which was created by USS internally, but was reviewed by its financial advisor in the transaction and was relied upon by the USS board of directors in connection with their decision to make the Acquisition.

[285] The financial model contemplated stable sales of flat-rolled steel that would rise 1%-2% annually, which would generate earnings before interest, taxes and depreciation ("EBITDA") estimated to be U.S. $368 million in 2008 and projected to gradually rise over the next seven years. Brockway testified that, based on this financial model, USS anticipated that the Acquisition would generate sufficient free cash flow in USSC to pay the interest provided for under the Term Loan and to repay the principal over the 30-year term of the Term Loan. The financial model also included a discounted cash flow analysis. The extent to which this analysis is also supportive of the USS expectation is unclear. However, there is no evidence regarding this financial model that contradicts USS's expectation of repayment of the Term Loan with interest.

[286] The Objecting Parties do not dispute that USS made its decision to acquire USSC based on the financial model described above. However, the Objecting Parties argue that the constellation of factors described above pertaining to the terms of the Term Loan Agreement, and the manner in which USS administered the Term Loan, demonstrate that USS did not expect to be repaid the principal with interest of the initial advances under the Term Loan.

Did USS Expect to be Repaid the Term Loan With Interest?

[287] I do not propose to revisit the considerations that have been excluded for the reasons set out in the preceding section, including, in particular, the considerations that rely on a comparison with a third-party lender standard. Setting those considerations aside, the position of the Objecting Parties is based primarily on the following remaining factors which will be evaluated without regard to a third-party lender standard: (1) the terms of the Term Loan Agreement, in

particular the deferred interest payment dates and the length of the term of the Term Loan; (2) the acceleration of interest payments in 2008; (3) the waivers of interest commencing in 2010; and (4) the view of the Objecting Parties that USS effectively subordinated payments on the Term Loan to payment of USSC's trade creditors. The Objecting Parties argue that, even considered without regard to the third-party lender standard, these factors, particularly the actions of USS after the advances were made, evidence the fact that USS did not expect to receive repayment of the principal with interest of the Term Loan. I will address each of these factors in turn and will then address the probative value of these factors considered collectively.

[288] First, as mentioned, the Term Loan Agreement provided USSC and USS with considerable latitude regarding the timing of both the payment of interest and the repayment of principal. There was a legitimate business reason for these terms of the Loans. They provided USS with some, but not complete, flexibility to align the payment of interest with the receipt of excess cash flow in a highly cyclical industry. They also provided a lengthy period of time over which to repay the Loans for the same reason. These terms were permissible under applicable tax legislation without losing the tax treatment for debt. For the reasons set out above, I do not think that the terms of the Term Loan Agreement, by themselves, are more consistent with a re-characterization of the Term Loan as a capital contribution. The mere existence of provisions providing flexibility in the timing of payment of interest and repayment of principal is not a basis for inferring that USS did not expect to receive repayment with interest of the Term Loan without further evidence at the time of the initial advances. There is no such evidence in this case. In particular, as noted above, there is no evidence regarding the financial model that establishes, on a balance of probabilities, that repayment of the Term Loan was not a realistic possibility over the life of the Loan.

[289] Second, the Objecting Parties suggest that the acceleration of interest payments in 2008 supports a finding that the payments were, in substance, dividend payments. For the reasons set out in the preceding section, I do not think that the two interest payments made in late 2008 are more properly characterized as dividends based on a third-party lender standard. I also do not think that the action of causing such payments in advance of their respective payment dates is, on its own, indicative of treatment of the Term Loan as a capital contribution. More generally, in the absence of any documentary or other evidence at the time of the payments suggesting otherwise, the fact that the payments were characterized as interest payments, that the payments did not exceed the amount of the accrued interest at the time, that the payments were permitted under the Term Loan Agreement, and that there was a legitimate business purpose for making interest payments in advance of their due date should be determinative.

[290] Third, the Objecting Parties' reliance on the interest waivers and failure to repay any interest in the seven years between the initial advances under the Term Loan and the Filing Date is understandable. It raises a legitimate question of whether USS ever intended USSC to pay principal or interest on the Term Loan, that is, whether it ever expected to be paid interest and/or repaid principal.

[291] There is some force to this argument in one respect. Insofar as USS waived, rather than continued to accrue, unpaid interest, it appears to have acted as a shareholder rather than a lender. The evidence before the Court established that it was not economic for USS to "round-trip" the payment of interest by USSC under the Term Loan. This explains why USS did not fund USSC to enable it to pay the accrued interest. However, it does not explain why it was

appropriate to write off the interest that was waived in each of the relevant years, much less why only a portion of the interest was written off. Moreover, based on an internal email dated March 29, 2011 of USS, it is possible that, in or about late 2010 or early 2011, USS decided on a policy of waiving at least some interest at the end of each year to the extent USS was not in a position to pay the accrued interest payable in such year.

[292] However, the Objecting Parties suggest that the Court should infer from the interest waivers that USS did not expect to receive repayment with interest of the Term Loan at the time of the initial advances under the Term Loan. In the preceding section, I addressed the argument of Dr. Finnerty that the Court should draw such an inference from USS' failure to assert its rights as a lender in respect of the interest payment defaults that gave rise to the interest waivers. In this section, I address the alternative argument of the Objecting Parties that the granting of the interest waivers by themselves is sufficient to support the inference that USS never expected to receive repayment of the Term Loan with interest at the time that the initial advances were extended thereunder.

[293] I do not think a court can reasonably draw such inferences for a number of reasons. First, and most important, there is no other evidence supporting such an expectation at the time of the establishment of the Term Loan and the making of the initial advances under the Loan. Second, the payment of interest under the Term Loan in 2008 is inconsistent with an absence of any expectation of payment of interest from the outset of the Term Loan. Third, the intervening economic events are sufficient to establish radically different economic conditions which support the USS position of altered expectations. There is no evidence that USS contemplated the possibility of a recession of the depth and length experienced in the steel market since 2008 even though it put in place flexibility regarding interest payments and a long maturity date as discussed above. Fourth, notwithstanding the waivers in 2011, 2012 and 2013, there is no evidence that such repeated waivers of interest reflected a long-term policy of USS that existed from the outset of the Term Loan.

[294] Accordingly, the significant facts for this purpose are the lengthy period after the initial advances before the initial decision was made to waive interest coupled with the intervening occurrence of significantly adverse market conditions. These factors, together with the absence of any documentation or other evidence to the contrary at the time of the initial advances under the Term Loan, exclude an intention at the time of such advances to waive interest as and when it became payable under the terms of the Term Loan Agreement.

[295] Lastly, with respect to the argument of subordination, I have concluded for the reasons set out above that the evidence regarding the alleged effective subordination of the Loan does not evidence the absence of an expectation of USS of repayment with interest of the Term Loan or the Revolver Loan, except to the extent of the waived interest which has been addressed above. I would add that I do not consider that the evidence of Brockway, discussed below, constitutes evidence that USS implemented a policy of subordination of the Term Loan to trade creditors from the time of the initial advances as the Objecting Parties suggest.

[296] The Objecting Parties have raised one further argument that should be addressed pertaining to the use of the initial advances under the Term Loan. They suggest that both the use of the advances under the Term Loan to acquire capital assets, being the Stelco shares and other Stelco securities, and the circumstances surrounding the SHC Transaction, argue for a finding

that the Term Loan constituted, in substance, a contribution to capital. I do not accept either submission for the following reasons.

[297] With respect to the significance of the acquisition of the Stelco shares and other securities, the Objecting Parties say that such use of the initial advances under the Term Loan demonstrates that the primary intention of USS was the acquisition of Stelco rather than the establishment of a debtor-creditor relationship between Canada LP and ABULC.

[298] This argument presumes that the purpose of debt is the provision of working capital and that the purpose of equity is the acquisition of capital assets. That is too narrow an approach. Term loans are regularly used to acquire capital assets and, indeed, are often secured on such capital assets in the case of third-party lenders. There is no necessary reason why the fact that advances under a term loan were used for the purpose of acquiring assets should be a consideration that demonstrates a capital contribution. In addition, as discussed above, there is no general principle that prevented USS from structuring a portion of its investment in USSC as a loan. Moreover, as described below, the portion of the Term Loan that reduced the Credit Corp Loan was effectively used to retire the third party debt of Stelco at the time of the Acquisition.

[299] With respect to the SHC Transaction, the Union argues that the fact that advances under the Term Loan were used to satisfy the Credit Corp Loan, which was incurred to refinance the Stelco debt at the USS level, is indicative of a view of the Term Loan as an equity contribution. I do not see the connection suggested by the Union.

[300] The SHC Transaction has been described above. The principal effect of the SHC Transaction was to effect a sale of SHC at its apparent fair market value by USSC and a reduction of the Credit Corp Loan in a like amount. If the SHC Transaction had not occurred, the Credit Corp Loan would have remained outstanding as of the Filing Date in the amount of such reduction and the amount of the Term Loan would have been correspondingly lower. From the point of view of the aggregate amount of outstanding debt of USSC, the SHC Transaction was therefore neutral. Moreover, the Credit Corp Loan was made for the purpose of repaying third-party debt of Stelco. To the extent that advances under the Term Loan in connection with the SHC Transaction were applied to reduce the Credit Corp Loan, such advances were therefore indirectly used to repay such third-party debt. I do not see any further significance to the SHC Transaction.

[301] It is therefore necessary to address the argument of the Objecting Parties that, while none of the foregoing factors or considerations may be sufficient on its own to support a conclusion that the Term Loan was, in substance, a capital contribution, the combination of factors should support such a conclusion. This argument effectively brings together all of the factors set out and discussed above and asserts that collectively they establish that it is more probable that USS did not expect to receive repayment with interest of the Term Loan than that USS had such an expectation.

[302] In considering this argument, I have looked more generally at which of the two scenarios proposed by the parties is more probable – the USS position that it expected to be repaid the principal with interest of the Term Loan at the time of the advances in 2007 or the Objecting Parties' position that, at the time of such advances, USS expected to receive only such cash flow and assets as were available after satisfaction of the obligations to third party creditors

and to write off the principal or interest in respect of the Term Loan when cash was not available and such obligations fell due.

[303] In addition to the factors described above, the Objecting Parties rely on the evidence of Brockway referred to above and the evidence more particularly described in certain excerpts of Brockway's discovery in these proceedings set out at pages 8 and 9 of the Union's Compendium of Key Read-in Evidence. The Union submits that these excerpts establish that USS' expectation of repayment was "contingent on USSC's performance" or was "dependent on the success of Stelco's business going forward" and that "[USS] only expected to receive interest payments if USSC was successful." I note that this argument is similar to, but separate from, the argument that USS effectively subordinated repayment of the Term Loan, and payment of interest thereon, to the payment of USSC's third party creditors.

[304] I do not think that this submission accurately captures the evidence of Brockway and, accordingly, I think that the Objecting Parties rely on an interpretation of his evidence which it was not intended to carry.

[305] There is a difference between the investment risks of USS' investment in Stelco, considered as a whole, and the risk of repayment of the portion of the investment that was structured as debt of USSC. Reading the entirety of Brockway's evidence, I am satisfied that Brockway's statement was intended to acknowledge no more than that there could be no certainty that the aggregate investment in Stelco would be profitable. Brockway acknowledged no more than that the Acquisition entailed normal investment risks and that, to the extent that USS made a bad investment, there was a risk that it had made such a bad investment that USSC would be unable to repay not only its equity investment but also the Term Loan with interest. His evidence does not, however, constitute an acknowledgement that USS believed it had made an unprofitable investment in acquiring Stelco, much less an acknowledgement that USS therefore expected that USSC would be unable to repay the Term Loan with interest.

[306] The foregoing discussion highlights the fact that, at times, the position of the Objecting Parties approaches the issue of repayment of the Term Loan as part of the larger issue of the profitability of the entire investment of USS in USSC. This is reflected in the position of the Union, as excerpted above, which proceeds on the basis that USS treated both the Loans and the equity component as a single investment. In so doing, the Objecting Parties disregard the reality that the Term Loan was expressly structured and documented separately from the equity injections in order to function in the manner described above. I do not think that the separate existence of the Term Loan can be simply ignored in the absence of an explanation or reason for treating the USS investment on an aggregate basis. In doing so, this approach conflates the issues of repayment of the Term Loan and the profitability of USS' acquisition of Stelco, which are very different. The Court is only concerned with USS' expectation of repayment with interest of the Term Loan. Even an unsuccessful investment may nevertheless repay with interest the portion of the investment structured as a loan.

[307] Further, to the extent that Brockway was also acknowledging the existence of lending risks with respect to repayment of the Term Loan, the mere existence of lending risks is not a basis for an inference that there was no expectation of repayment of the debt portion of the USS' investment in USSC. The statement that USSC would not be able to repay the Term Loan with interest unless it was profitable is, on its own, a neutral statement. There is a considerable

distance between an acknowledgement of the existence of normal lending risks and an acknowledgement that USS did not expect USSC to be able to repay the Term Loan with interest. I do not read Brockways' testimony as going to the latter statement.

[308] It is also necessary to address the position of the Province as excerpted above. The Province argues, in effect, that, having made the decision to acquire Stelco and to integrate it into the USS business as an operating division, USS paid no attention to the ability of USSC to repay the Term Loan over the thirty-year life of the Loan. It says that such action demonstrates that the Term Loan was, in effect, equity. By way of explanation for this approach, the Province suggests that USS considered the investment from a business-wide perspective. The Province suggests that USS was not concerned specifically with the profitability of USSC, and its ability to repay the Term Loan, given that USS considered that an increased profitability of other companies within the USS group would more than compensate for any losses in USSC.

[309] At the time of the initial advances under the Term Loan, USS undoubtedly intended to integrate Stelco into its business as an operating division. That fact alone, however, does not support the conclusion that USS had no expectation that USSC would be unable to repay with interest the portion of the acquisition cost that was provided to it in the form of the Term Loan. More importantly, the evidence does not support the conclusion that USS paid no attention to the ability of USSC to repay the Term Loan in the manner suggested by the Province for the following reasons.

[310] First, as Brockway noted, it is incorrect to suggest that USS made no credit analysis of USSC in connection with the initial advances under the Term Loan. The financial model, upon which the decision to acquire Stelco was based, served the function of a credit analysis even if the principal purpose of the model was to address the financial impact of the entire investment. In its projections of cash flows of the post-acquisition Stelco, the financial model provided the basis for a conclusion regarding USSC's ability to service the Term Loan. As set out below, the evidence before the Court with respect to this financial model does not demonstrate that USS did not expect to receive repayment with interest of the initial advances under the Term Loan over the life of the Loan.

[311] Second, while the financial model did anticipate the realization of substantial synergies outside of USSC, it is not suggested that the quantum of such synergies was such that they would compensate for anticipated losses in USSC. More generally, there is no evidence that USS did not anticipate recovery of the majority of its investment in the form of profits from USSC, including the portion represented by the initial advances under the Term Loan which for this purpose is notionally senior to USS' equity investment.

[312] The Brockway evidence therefore does not constitute an acknowledgement or admission of USS that it had no expectation of repayment with interest of the initial advances under the Term Loan when they were made. For the reasons set out above, I am also not persuaded by the Province's argument that USS allocated its investment in Stelco between debt and equity with no regard to USSC's ability to repay the initial advances under the Term Loan. The probative value of the other considerations upon which the Objecting Parties rely has been discussed above. The element of USS' actions which most strongly raises a doubt regarding its expectation regarding repayment of the Term Loan is the experience of the interest waivers. The Objecting Parties also rely, among other considerations, on the long maturity date, the absence of

a schedule of repayments, and the alleged effective subordination. For the reasons set out above, however, none of this evidence is sufficient on its own to support a characterization of the Term Loan advances as equity. I am also not persuaded, for the reasons discussed above, that the experience of the interest waivers, together with the other considerations upon which the Objecting Parties rely, collectively demonstrate that USS did not expect to be repaid the initial advances under the Term Loan with interest as of the time such advances were made in 2007.

[313] Accordingly, I find, on a balance of probabilities, that, at the time of the advances under the Term Loan in 2007, USS expected that USSC would repay interest on the Term Loan in accordance with the terms of the Term Loan Agreement and would repay principal on or prior to the maturity date of the Term Loan.

Was the USS Expectation Reasonable?

[314] This raises the issue of the reasonableness of the USS expectation.

[315] The Objecting Parties rely heavily on two factors which might suggest that such an expectation was unreasonable: (1) third party financing was not available to USSC on terms substantially similar to the terms of the financing provided by USS; and (2) the view of the Objecting Parties that ABULC was inadequately capitalized. I will address these issues in turn.

[316] As mentioned, the Province introduced the Hall Report as expert evidence demonstrating that a third party lender would not have provided ABULC/USSC with financing in the amount and on the terms of the Term Loan provided by USS.

[317] There is no actual dispute regarding this opinion in the Hall Report. However, for the reasons set out above, the standard addressed in the Hall Report — i.e., whether USSC could have obtained financing on the terms and in the amount of the Term Loan from a bank or other institutional lender — is too limited to establish that the USS expectation of repayment of the Term Loan was unreasonable. In this regard, it is noteworthy that both Mr. Hall and Dr. Finnerty, who relied on the Hall Report for the purpose of the opinion in the Finnerty Report on this issue, acknowledged that they were not expressing any opinion on the ability of USSC to have obtained financing other than from a third-party lender.

[318] The question remains whether the evidence regarding the ability of USSC to raise debt on a viable basis as of December 31, 2007 contradicts the reasonableness of the USS expectation. If the Objecting Parties were able to demonstrate, on a balance of probabilities, that USSC could not have obtained external financing in the amount of the Term Loan on any viable basis, I think a court could conclude that at least the excess of the Term Loan over the amount of financing that was obtainable from external sources represented an equity contribution.

[319] However, in the present circumstances, the evidence is not sufficient to establish that USSC lacked the capacity to raise an amount of debt equal to the outstanding amount of the Term Loan as of December 31, 2007, that is, that external financing would not have been available to USSC on a viable basis, although admittedly on a fully secured basis. Accordingly, the Objecting Parties cannot establish that the USS expectation in 2007 of repayment with interest of the Term Loan was unreasonable. In this regard, the following considerations are relevant.

[320] First, Stelco had total debt approximating $1.16 billion at the time of the Acquisition. As the Austin Smith Report suggests and Mr. Hall acknowledged, this would appear to put a floor on the debt capacity of USSC at the time of the Acquisition.

[321] Second, the historical financial results for Stelco (EBITDA and EBIT) prior to the Acquisition, when adjusted to remove non-recurring items, reflected an improving trend from 2006 to 2007 on a quarter-over-quarter comparison by year.

[322] Third, the outstanding balance of the Term Loan at December 31, 2007, being approximately $1.4 million including the outstanding loan from the Province, was not significantly higher than the amount of the Stelco debt prior to the Acquisition. This level of debt represented approximately 70% of the total acquisition cost to USS of Stelco. It is not inconsistent with Brockway's testimony that USS believed that the Term Loan could be repaid over the 30-year life of the Loan as Brockway suggested. It is true that the investment failed to generate the results contemplated by the USS financial model. By any estimation, in hindsight, the investment was a significant failure. However, there is no basis for retrospectively fixing USS with such knowledge at the time of the initial advances under the Term Loan.

[323] Fourth, the Hall Report bases its conclusions entirely on the historical performance of Stelco rather than on an analysis of the projected cash flow of USSC at the time of the Acquisition. However, as the Province's financial advisor in respect of the Acquisition, Ernst & Young Inc., recognized in a report dated August 22, 2007 to the Province, the Acquisition was likely to improve the financial strength of USSC relative to Stelco. The report identified a number of factors for consideration by the Province regarding the Acquisition. Purely from a cash-flow perspective, these factors would have been expected to result in an increased and more stable cash flow, other economic factors being equal. There is, therefore, a reasonable basis for concluding that the Acquisition increased USSC's debt capacity relative to Stelco's pre-Acquisition debt capacity. The fact that a third-party lender might not have been prepared to rely on USS' cash flow projections is not determinative of whether lenders in other capital markets were prepared to do so.

[324] Fifth, the limited metrics in evidence do not suggest that USSC lacked the ability to incur such external financing. As noted by Brockway, in 2007, Stelco incurred slightly less than $60 million in interest expense for the nine months ended September 30, 2007, or slightly less than $80 million on an annualized basis. The Term Loan interest for 2008 approximated $100 million, which was well within the estimated EBITDA for that year.

[325] Sixth, while the Acquisition was not a leveraged buyout transaction as that term is generally understood, USS, as a strategic purchaser, approached the purchase of Stelco with a similar philosophy and approach to capitalization, as the Austin Smith Report notes. In this regard, the financial metrics pertaining to aggregate debt and interest coverage, on a prospective basis, are consistent with leveraged buyout financing transactions in 2007 and are, therefore, suggestive of the availability of financing in the high-yield market.

[326] Given these factors, the evidence suggests a reasonable possibility of obtaining third-party financing in other capital markets, beyond the third-party lender market addressed in the Hall Report and the Finnerty Report, in particular, in the high-yield market. For the reasons discussed above, it is not relevant for present purposes that any such financing would have been

on different terms and conditions from the Term Loan. The second issue raised by the Union in its Factum is the allegedly inadequate capitalization of ABULC/USSC at the time of the initial advances under the Term Loan.

[327] Insofar as the Union says that ABULC was inadequately capitalized, I think the issue is misdirected. While it is correct that ABULC had no prior operating performance and no revenues or profits of its own, that is irrelevant. At all times, ABULC was the direct parent corporation of USSC. Its financial performance on a consolidated basis was that of USSC. Accordingly, the extent to which ABULC was or was not undercapitalized was directly dependent on the extent to which USSC was or was not undercapitalized.

[328] Insofar as the Objecting Parties say that post-Acquisition USSC was inadequately capitalized, I think this issue engages the same issue as the preceding discussion of the availability of external financing. To the extent that the evidence fails to establish that USSC could not have obtained external financing on a viable basis in the amount of the Term Loan, it cannot reasonably be argued that USSC was inadequately capitalized.

[329] Based on the foregoing, I find that the Objecting Parties have not satisfied the onus of demonstrating that the USS expectation of repayment with interest of the principal of the Term Loan as of December 31, 2007 was unreasonable.

Term Loan Advances in 2009

[330] As mentioned, in 2009, USSC received additional advances totalling $211.2 million under the Term Loan from Canada LP. No interest or principal was paid during 2009. In addition, as set out in the table above, USS provided equity injections in the amount of $61 million during 2009.

[331] The Objecting Parties do not raise any arguments regarding these advances under the Term Loan in addition to those addressed above. The relevant facts are essentially the circumstances as of December 31, 2007 carried forward, subject to the interest payments in 2008 and the occurrence of the recession in 2009. Given the history of the steel market in the period 2004 to 2008, USS had a reasonable expectation that markets would improve that justified supporting USSC in 2009 with additional working capital advances. I note as well that the first interest waiver under the Term Loan occurred subsequent to the advances in 2009.

[332] Accordingly, I see no basis for reaching a different conclusion respecting the expectation of USS regarding repayment of these advances from the conclusion reached above regarding repayment of the initial advances under the Term Loan. The evidence before the Court establishes that USS expected that USSC would repay these advances with interest for the reasons set out above. Hindsight is always 20/20. There is, however, no evidence that, as of 2009 when such advances were made, USS or USSC anticipated the negative financial performance of USSC in the period 2009 to 2013 and therefore expected that USSC would be unable to repay these advances with interest. There is also no evidence before the Court that would demonstrate that the expectation of repayment with interest of these advances under the Term Loan was unreasonable.

Conclusion Regarding Characterization of the Term Loan

[333] Based on the foregoing, I conclude that the outstanding Term Loan, being Claim #9, constitutes a debt claim rather than an "equity claim" for the purposes of this CCAA proceeding.

Analysis and Conclusions Regarding the Re-characterization Claim in Respect of the Revolver Loan

[334] I propose to set out my analysis of the debt re-characterization claim of the Objecting Parties with respect to the Revolver Loan after first setting out the position of the Objecting Parties in their written submissions. As in the case of the Term Loan, the Objecting Parties concentrated on a subset of these considerations at the trial, which are addressed in these Reasons.

Positions of the Parties

The Union

[335] The approach of the Union, as excerpted above from its written submissions, applies equally to the Term Loan and the Revolver Loan and therefore will not be repeated here. In its factum, the Union argues that the Revolver Loan should be re-characterized as equity based principally on the following seven *AutoStyle* factors: (1) the inability of USSC to obtain similar financing from outside lending institutions; (2) the source of repayments of the Revolver Loan; (3) the presence or absence of a fixed maturity date and schedule of payments; (4) the absence of security for advances under the Revolver Loan; (5) the absence of a sinking fund to provide for repayments; (6) the extent to which the advances under the Revolver Loan were effectively subordinated to the claims of outside creditors; and (7) the financial position of USSC, including an inadequate capitalization, at the date that the Revolver Loan was first put in place.

The Province

[336] The Province's approach, as excerpted above from its factum, also applies equally to the Term Loan and the Revolver Loan and therefore will not be repeated here. In its written submissions, the Province argues that the Revolver Loan should be re-characterized as equity based principally on two assertions also made in respect of the Term Loan, namely: (i) there was no expectation that USSC would repay the principal of the Revolver Loan advances; and (ii) the Revolver Loan was not provided by, nor available from, a third-party lender on commercial terms. The Province also suggests that the following three attributes of the Revolver Loan further demonstrate that it is, in substance, equity rather than debt: (1) the arrangements pertaining to interest including, in particular, determination of the interest rate based on tax requirements, the timing of interest payments in the loan agreements, and the reliance on equity injections to make interest payments under the Revolver Loan; (2) thin or inadequate capitalization of USSC at the date of the Revolver Loan Agreement and USSC's operating performance at the time; and (3) the failure to establish a sinking fund for repayment.

USS

[337] USS submits that the same *AutoStyle* factors upon which it relies in respect of the Term Loan also refute the Objecting Parties' re-characterization claim in respect of the Revolver Loan. Accordingly, I will not repeat them here.

Analysis and Conclusions

[338] The claim of the Objecting Parties that the Revolver Loan should be characterized as an "equity claim" also requires addressing the two matters discussed above: (1) the expectation of USS regarding repayment of principal with interest on the Revolver Loan out of cash flows of USS over the term of the Revolver Loan; and (2) the reasonableness of such expectation. In the case of the Revolver Loan, it is necessary to address these issues separately in respect of each of the First Tranche Indebtedness and the Second Tranche Indebtedness. Accordingly, I will deal with each Tranche in order.

The First Tranche Indebtedness

Background

[339] As set out above, the amount of the First Tranche Indebtedness outstanding as of October 31, 2013 was U.S. $116,969,996. It is understood that no payments of either principal or interest were made in respect of the First Tranche Indebtedness after October 30, 2013. The history of advances and payments under the Revolver Loan to this date is important for the determinations herein. The Monitor's Seventh Report sets out all such advances and repayments in Exhibit "O" thereto, which is briefly summarized as follows.

[340] During 2010, USSC drew a total of U.S. $100,000,000 under the Revolver Loan and made no interest payments. In 2011, USSC drew U.S. $20,000,000 in June, repaid U.S. $18,339,563 in November and drew U.S. $25,223,983 in December. In the same year, USSC paid U.S. $6,660,437 of interest in November and U.S. $223,983 of interest in December. As of December 31, 2011, the amount outstanding under the Revolver Loan was U.S. $127,155,598.

[341] In 2012, USSC obtained advances totaling U.S. $307,366,090. Advances were made in each month, other than March and April when it repaid U.S. $33,866,386 and U.S. $9,568,279, respectively, and October when there was no activity. In addition, small amounts of interest were paid in each of January, March and April, being U.S. $366,090, U.S. $1,133,614 and U.S. $431,721, respectively. At the end of December 2012, the outstanding balance of the Revolver Loan was U.S. $496,702,434, which amount was increased by a draw of U.S. $10,000,000 in early January 2013 to bring the outstanding amount to U.S. $507,750,128.

[342] As Dr. Finnerty observed, with the qualification that money is fungible, it can be argued that the payments on account of principal and interest in the aggregate amount of U.S. $25,000,000 in November 2011, and a further interest payment of U.S. $223,983 in December 2011, were funded by an equity injection in October 2011. It can also be argued that the payments on account of principal and interest in March and April 2012 were funded by an advance under the Revolver Loan in February 2012.

[343] In 2013, as described above, USS implemented a decision to "de-lever" USSC by reducing the Revolver Loan. Accordingly, principal and interest payments totaling $383,845,848 and $11,154,152, respectively, were made in each of the months of February to July 2013 inclusive. By this means, the balance outstanding at October 31, 2013, prior to the execution of the Third Revolver Amendment and the October Security Agreement, had been reduced to the level set out above, being the amount of the First Tranche Indebtedness. Applying advances and

repayments on a first-in, first-out basis, the advances outstanding under the First Tranche Indebtedness at the Filing Date were advances made in the course of 2012.

[344] It is necessary to overlay the economic performance of USS and USSC during these years. As described above, the evidence establishes that market conditions improved in the second quarter of 2010 and then weakened again in the second half of 2010. Similarly, market conditions improved in the second quarter and third quarter of each of 2011 and 2012 before weakening again in the fourth quarter of each year. Essentially, the evidence is that USS thought that the improvement in the markets in the first half of 2010 signalled the start of an improving market whereas, in retrospect, it heralded the beginning of several years of "mini-cycles" in each of 2010, 2011 and 2012. The evidence also indicates that a similar improvement did not occur in the first half of 2013.

[345] Exhibit "O" to the Monitor's Seventh Report sets out the equity injections made by USS during the period 2010 to October 2013 on a monthly basis, which is briefly summarized as follows. In 2010, USS made equity injections in each of June, July, September, October and December totaling $611,754,000. In 2011, USS made equity contributions in each of January, February, July, August, September and October totaling approximately U.S. $213 million. There were no equity injections in 2012. In 2013, as described above, in connection with its "de-leveraging" decision, USS contributed a total of $682,758,200 through equity injections in each month from February to and including September. It is not disputed that a significant portion of these equity injections in 2013 was used to pay interest owing, and to repay principal outstanding, on the Revolver Loan in connection with the "de-leveraging" exercise. A further $57,040,500 was injected in October 2013 prior to execution of the Third Revolver Amendment prompting a moratorium on further cash payments to USSC imposed by the new chief financial officer until security was provided.

Analysis and Conclusions

[346] The evidence indicates that USS established the Revolver Loan in May 2010 during a period of improvement in market conditions after the significant slowdown in business activity during the second half of 2008 and 2009. The funding under the Revolver Loan provided additional working capital required to respond to the recovery of the steel market that was anticipated at that time. As mentioned, the advances comprising the First Tranche Indebtedness were made in 2012 based on a first-in, first-out approach to advances and repayments under the Revolver Loan. Accordingly, such advances must be considered in the context of the economic environment in which they were made in 2012.

[347] USS says that it expected to be repaid all advances, with interest, when they were made under the Revolver Loan over the course of the Loan. As set out above, the principal argument of the Objecting Parties is that the terms of the Revolver Loan, as well as the manner in which the Loan was administered by USS, are more consistent with receipt of the residual cash flow and assets of the USSC, without any expectation of repayment with interest of the advances under the Revolver Loan.

[348] The Objecting Parties rely largely on the general considerations that were addressed in respect of characterization of the Term Loan. This is consistent with the fact that the Revolver Loan performed the same cash management function as the Term Loan. They also rely on certain

other considerations that are specific to the circumstances in which the First Tranche Indebtedness was advanced. These include the following matters: (1) the losses of USSC since 2009; (2) the failure of USSC to pay any interest on the Term Loan after 2009; (3) the negative equity of USSC in 2012; (4) the removal of the solvency representation from the Revolver Loan; and (5) the use of equity injections to fund repayment of the Revolver Loan pursuant to the "de-leveraging" exercise described above in 2013.

[349] I will first address the application of the general considerations that the Objecting Parties suggest demonstrate the equity character of both the Term Loan and the Revolver Loan and then the additional considerations which they raise that are specific to the Revolver Loan.

[350] As mentioned, in the period from 2010 to 2012, that is, prior to the "de-leveraging" exercise discussed below, USS administered the Revolver Loan in the same manner as it had administered the Term Loan with the exception that: (1) in each of 2011 and 2012, USSC repaid some principal and paid some accruing interest out of available cash; and (2) USSC did not waive any interest that became payable during this period. There are no additional facts in respect of the administration of the Revolver Loan that render the combined effect of the general considerations upon which the Objecting Parties rely more compelling in the context of the Revolver Loan than the Term Loan.

[351] I therefore do not think that the terms of the Revolver Loan Agreement and the manner in which USS administered the Revolver Loan are sufficient to constitute the Revolver Loan, in substance, an equity contribution. There is nothing in these circumstances, considered on their own or collectively, that casts any doubt on the evidence that USS expected USSC to repay the principal with interest of the First Tranche Indebtedness over the life of the Loan.

[352] The next issue is therefore whether the financial status of USSC in 2012, when the advances comprising the First Tranche Indebtedness were made, affects this conclusion. The Objecting Parties say that the Court should infer from the four considerations set out above, which pertain to the financial state of USSC in the latter half of 2012, that USS did not expect to receive repayment with interest of the Revolver Loan. These factors raise a legitimate issue regarding both the expectation of USS and the reasonableness of that expectation at that time. I propose to address the issue of the removal of the solvency representation first and then the remaining considerations pertaining to USSC's financial state.

[353] The Objecting Parties place considerable reliance on the agreement of USS to remove the solvency representation from the Revolver Loan Agreement in 2012 as evidence that USS could not have expected USSC to be able to repay any advances under the Revolver Loan. The solvency representation was removed by the First Revolver Amendment in July 2012 at the request of Michael McQuade, the chief financial officer of USSC at the time ("McQuade").

[354] McQuade states in his affidavit sworn September 4, 2014 that, at the time of the execution of the First Revolver Amendment, he had a concern about USSC's solvency given its losses since 2009 and its reliance on USS for on-going liquidity and solvency. He testified at the hearing of this motion that he had a concern that USSC might become insolvent at some point over the remaining thirteen-year term of the Revolver Loan.

[355] The Objecting Parties suggest the Court should draw the inference that USS was aware that USSC was insolvent in July 2012 and, from that inference, find that USS had no expectation of repayment with interest of the advances made in 2012 under the Revolver Loan. I do not think the evidence justifies such an inference or finding for the following reasons.

[356] First, there is no evidence regarding the intentions of either USS or USSC in removing the insolvency representation that supports such a finding. McQuade requested its removal. His evidence at the trial was that he approached the solvency representation as a continuing representation. McQuade's concern was prospective rather than immediate. He was concerned that USSC might breach the representation at some point in the future rather than that USSC was insolvent in July 2012. In addition, McQuade also testified that he believed that USSC had a continuing right under the Revolver Loan Agreement to draw funds as needed up to the maximum availability. It is not clear how he integrated these two apparently contradictory considerations. McQuade's view of the operation of the Revolver Loan Agreement does, however, reinforce the prospective nature of his concern. In addition, there is no evidence regarding why USS agreed to remove the solvency representation at the time.

[357] Second, it is not possible to draw any conclusion regarding the knowledge of USS and USSC from the terms of the Revolver Loan Agreement for the following reasons. As described elsewhere in these Reasons, I consider that the proper interpretation of the Revolver Loan Agreement is that a balance sheet solvency test remained in the form of the "unable to meet debts" event of default. In addition, a similar event of default remained in the Term Loan Agreement. I do not see any inconsistency in the removal of the solvency representation and the retention of a balance sheet event of default. Moreover, it is not clear whether the solvency representation was a continuing representation given at the time of each advance. Even if it was, which may be more likely, the net effect of the amendment was to remove the solvency test based on meeting liabilities as they fell due. As discussed above, there was no need for such an event of default in the context of a wholly-owned subsidiary relationship. It is therefore questionable whether the removal of the insolvency representation had any real practical significance from which it would be possible to draw an inference.

[358] Third, while USSC may not have been solvent on a book value basis in July 2012, there is no evidence to suggest that USS considered that USSC was insolvent on a market value basis at that time, which is the relevant issue both as a practical matter as well as a legal matter.

[359] I turn then to the remaining financial performance considerations upon which the Objecting Parties say that the Court should infer an absence of an expectation of repayment of the Revolver Loan on the part of USS in 2012. With hindsight, these considerations point in the direction of continuing financial problems of USSC which were identified in the autumn of 2013. With the benefit of that hindsight, it is also clear that USS had very lax controls over the provision of additional cash to USSC from 2010 until late October 2013 and perhaps poor planning processes. In practice, USSC's requests, as set out in its rolling thirteen-week cash forecasts, appear to have been satisfied on a regular basis without close scrutiny by the USS treasury department.

[360] However, such evidence, considered collectively with the other considerations relied upon by the Objecting Parties, is not sufficient to establish that USS actually expected that USSC would be unable to repay with interest the advances in 2012. The evidence is more consistent

with a USS expectation that funding additional working capital in 2012 was appropriate given an anticipated improvement in the steel market, with a concomitant ability of USSC to repay such advances under the Revolver Loan as USSC returned to profitability.

[361] The advances under the Revolver Loan funded USSC with a view to increasing its working capital to take advantage of more favourable steel markets that were expected at the time. As described above, there were mini-cycles in each of 2010, 2011 and 2012. In each case, USS misread these mini-cycles as the start of a more broad-based improvement that did not occur. In the case of these advances, the evidence indicates a misplaced belief that the performance of USSC would improve in 2012 and 2013. There is, however, no evidence before the Court which suggests that USS did not hold these views. Nor is there any evidence that such views were unreasonable at the time.

[362] The Objecting Parties also raise the issue that the outstanding principal amount of the Revolver Loan was reduced from slightly in excess of U.S. $500,000,000 to the amount of U.S. $116,969,996 during 2013 pursuant to the "de-leveraging" exercise that was funded by equity injections from USS. They suggest that the source of funds is a factor indicating that the Revolver Loan was, in fact, an equity injection. There are three difficulties with this argument.

[363] First, USS had a legitimate business purpose in reducing the outstanding amount of the Revolver Loan that was not connected in any way to its expectation regarding the ability of USSC to repay the Revolver Loan. The "de-leveraging" exercise was undertaken to remove foreign currency fluctuations from the USSC financial statements and, thereby, to address an unnecessary complication in the USS consolidated financial statements.

[364] Second, in any event, I do not see any necessary connection between the use of the equity injections to reduce the outstanding balance of the Revolver Loan and the characterization of the remaining outstanding balance of the Loan. It may be that the use of equity injections reflected the fact that, in the course of 2013, USS concluded that USSC was no longer likely to be able to repay an amount of the Revolver Loan equal to the amount repaid by the equity injections. However, any determination to that effect would require evidence regarding the options available to USS to address the currency fluctuation issue, including the feasibility of conversion of such advances into another debt instrument rather than equity. Such evidence was not before the Court. In addition and in any event, the issue for the Court is whether USS expected repayment of an amount of the Revolver Loan equal to the remaining balance, being the First Tranche Indebtedness. The "de-leveraging" exercise does not demonstrate that USS also concluded that USSC would not be able to repay the amount of the Revolver Loan that it determined to leave outstanding.

[365] Third, there is a significant element of hindsight to this particular argument. The advances comprising the First Tranche Indebtedness were fully advanced before a decision to undertake the "de-leveraging" exercise was taken. In the absence of any documentary evidence of USS' decision-making in 2012, it is not possible to establish that the USS decision to convert a portion of the Revolver Loan to equity in 2013 reflected a determination made earlier in 2012 at the time of the advances under the Loan regarding the ability of USSC to repay such advances. More generally, there is no evidence that demonstrates that the use of equity injections to repay a portion or all of the Revolver Loan was contemplated at any time prior to late January 2013.

[366] Accordingly, I do not see any demonstrable connection between the use of the equity injections to pay down the Revolver Loan and the expectation of USS regarding repayment with interest of the Loan when the Revolver Loan was established or when the advances comprising the First Tranche Indebtedness were made in 2012.

[367] Lastly, as mentioned, the Province argues that, in respect of the Revolver Loan, USS advanced monies to USSC as an operating division based on anticipated benefits to the overall USS business and without any expectation of the payment of interest or the repayment of principal of the advances. On this view, USS provided monies to USSC that would not earn interest or be repaid because it would earn sufficient additional profits elsewhere in the organization to justify the increased equity investment in USSC.

[368] While such a possibility cannot be wholly discounted, the evidence for such a conclusion is lacking, apart from the absence of any credit analysis by USS before establishing the Revolver Loan in 2010, upon which the Province relies. There is no evidence that the losses that USSC generated were compensated for by profits elsewhere within the USS companies between 2010 and 2012. Moreover, there also is no evidence that, by 2010, the synergies envisaged at the time of the Acquisition outside of USSC were being realized within the USS business. As discussed above, the evidence only goes as far as demonstrating lax controls and perhaps a poor planning process. Such evidence is insufficient to demonstrate an absence of an expectation of repayment with interest of the advances under the Term Loan.

[369] Based on the foregoing, I therefore find that the evidence demonstrates, on a balance of probabilities, that USS had an expectation of repayment with interest of the advances comprising the First Tranche Indebtedness at the time such advances were made.

[370] I turn then to the evidence regarding the reasonableness of such expectation.

[371] In this regard, the principal argument of the Objecting Parties is that USSC could not have obtained an operating loan from a third-party lender on the terms and conditions of the Revolver Loan. They argue that this fact demonstrates that the First Tranche Indebtedness was in substance an equity injection.

[372] There is no doubt that a third-party lender would not have made an operating line of credit available on the terms and conditions of the Revolver Loan. The Hall Report opines that a third-party lender would not have granted an unsecured credit facility in 2010 given the circumstances that USSC was unprofitable, was experiencing negative EBITDA, had a net worth deficit on a book value basis, and had an outstanding balance under the Term Loan of approximately $1.6 billion. On the other hand, there is no evidence before the Court that would support a conclusion that secured financing would not have been available on viable terms from an external source other than a third-party lender. Neither Mr. Hall nor Mr. Finnerty expressed any opinion on this matter.

[373] The more difficult question is whether any external financing would have been available given the amount outstanding under the Term Loan in 2012, that is, whether the total debt capacity of USSC would have been exceeded by the addition of a secured operating line. If it could be demonstrated that such financing would not have been available, a court could find

that it was unreasonable to expect repayment of the advances of the First Tranche Indebtedness, being Claim #10, when they were made.

[374] However, there is no capital markets evidence before the Court that addresses this issue directly.

[375] The limited financial evidence referred to above is not sufficient to support any inference regarding the debt capacity of USSC at such time as it is limited to the availability of an unsecured revolver loan from a third-party lender. As the Objecting Parties bear the onus of proof, there is, therefore, no basis for a conclusion that USS' expectation of repayment was unreasonable on the basis that USSC lacked the aggregate debt capacity in 2012 to establish a revolving loan facility in the amount of the Revolver Loan.

[376] Based on the foregoing, I conclude that USS had a reasonable expectation of repayment with interest of the advances constituting the First Tranche Indebtedness at the time such advances were made. I therefore also conclude that the unsecured Claim in respect of the Term Loan, being Claim #10, constitutes a debt claim rather than an "equity claim" for the purpose of this CCAA proceeding.

The Second Tranche Indebtedness

[377] As set out above, Credit Corp advanced loans to USSC under the Revolver Loan totaling U.S. $71 million after the execution of the Third Revolver Amendment and the October Security Agreement on or about October 30, 2013. These advances were outstanding at the Filing Date. USS did not make any equity injection after October 30, 2013. As noted above, USSC acknowledges that USSC was insolvent on a balance sheet basis as of October 31, 2013, by which it is understood that USSC's liabilities exceeded the fair market value of its assets as of that date. The Objecting Parties argue that the Second Tranche Indebtedness was also an equity contribution.

[378] For clarity, I have approached the issue of characterization of the Second Tranche Indebtedness on the basis that such Indebtedness is secured by the security constituted by the October Security Agreement. Because USS required such security before advancing the Second Tranche Indebtedness, it is not realistic to address the characterization of such Indebtedness independently of such security. Accordingly, no conclusion is reached in these Reasons on the characterization of such Indebtedness to the extent that such security may be held to be void or unenforceable.

[379] I find the evidence supports the conclusion that USS expected to be repaid the Second Tranche Indebtedness as advanced under the Revolver Loan for the following reasons.

[380] First, there can be little doubt that USS expected to be repaid the advances made after October 30, 2013 with interest given the security over all the assets of USSC provided by the October Security Agreement. The existence of security for the Second Tranche Indebtedness overwhelms any argument that could be made for an absence of any expectation of repayment with interest based on the general considerations relied upon to seek to characterize the Term Loan and the First Tranche Indebtedness as capital contributions. The existence of security also

precludes an argument based on the financial status of USSC at the time the advances comprising the Second Tranche Indebtedness were made.

[381] Second, the principal argument of the Objecting Parties is that USS was legally and practically obligated to continue funding USSC. The Objecting Parties say that, if USS had not funded through the Revolver Loan, it would have had to fund the same amounts by equity injections. They argue that therefore the Revolver Loan was effectively an equity contribution. There are two difficulties with this argument.

[382] First, I find that USS was not legally obligated to continue funding USSC under the Revolver Loan Agreement for the following reasons.

[383] The Objecting Parties submit that, as of October 31, 2013, USS was legally obligated to continue to make all advances requested by USSC up to the limit of the availability under the Revolver Loan Agreement, being U.S. $600 million. This position is based on the contractual interpretation set out in the Di Massa Report of the "unable to meet debts" event of default in section 11c of the Revolver Loan Agreement as of October 30, 2007.

[384] However, I have concluded above that the "unable to meet debts" event of default constituted a balance sheet insolvency event of default in the Revolver Loan Agreement. There is no dispute that USSC was insolvent on a balance sheet basis in October 2013. Accordingly, on this interpretation of the Revolver Loan Agreement, an event of default had occurred under the "unable to meet debts" event of default in the Agreement entitling USS to refuse to advance further funds to USSC thereunder.

[385] In addition, even assuming that USS was obligated practically to ensure financing for USSC, I do not think it is correct to say that USS was obligated to provide that financing by equity injections. This argument assumes that secured financing was not available from external sources on a viable basis in the amount of the Second Tranche Indebtedness. However, there is no reason to think that a revolving loan on a secured basis in the amount advanced during the remainder of 2013, being approximately $71 million, would not have been available to USS, although admittedly on terms and conditions which would have differed from those of the Revolver Loan.

[386] I note that the Objecting Parties acknowledged at the trial that, but for the foregoing argument, they would have no compelling argument for characterization of the Second Tranche Indebtedness as a capital contribution. In particular, they do not raise any argument to the effect that any expectation of USS of repayment of the Second Tranche Indebtedness as secured debt was unreasonable. The principal issue raised by the Objecting Parties in respect of the Second Tranche Indebtedness is the validity or enforceability of the security for such Indebtedness constituted by the October Security Agreement, which is discussed below.

[387] Based on the foregoing, I conclude that USS had a reasonable expectation of repayment with interest of the advances comprising the Second Tranche Indebtedness at the time such advances were made.

The Validity of the Security for the Second Tranche Indebtedness

[388] The Objecting Parties submit that the security for the USS Secured Claims (being, collectively, Claims # 11, 11(a), 11(b), and 11(c)) should be invalidated. They make two principal arguments: (1) that the October Security Agreement and the November Security Agreement are unenforceable for lack of consideration at the time that they were executed and delivered by USSC; and (2) that the October Security Agreement and the November Security Agreement are void as constituting a fraudulent preference for the purposes of section 95(1)(b) of the BIA.

[389] In this section, I will address these issues in respect of the security for the Second Tranche Indebtedness, being the October Security Agreement. The security for the Remaining USS Secured Claims will be addressed in the last section of these Reasons.

Alleged Unenforceability of the October Security Agreement

[390] The Province and the Union argue that the October Security Agreement is unenforceable due to a lack of consideration at the time that it was executed and delivered by USSC and submit that, accordingly, the security constituted by such Agreement is invalid. On this basis, they argue that USS Claim #11, being the Second Tranche Indebtedness, should be declared to be an unsecured claim.

[391] USS says consideration was given for the October Security Agreement in the form of further advances under the Revolver Loan which would not have been granted without the provision of security for such advances, as referenced in the recital in the October Security Agreement cited above.

[392] The position of the Objecting Parties raises the following issues pertaining to the validity of security:

1. Is consideration for the October Security Agreement necessary for an enforceable security interest?

2. If so, did USS give consideration for the October Security Agreement in the form of an agreement to advance further funds under the Revolver Loan?

3. Alternatively, did USS give consideration for the October Security Agreement in the form of a forbearance or a waiver in respect of USS' rights to declare a default or take enforcement proceedings pursuant to the Revolver Loan Agreement or otherwise?

[393] I do not accept the position of the Objecting Parties that the October Security Agreement is unenforceable for want of consideration for the following reasons, which address each of these questions in turn.

[394] First, I do not think consideration is required for a grant of a security interest to be effective, although it will not be enforceable until such time as an obligation arises in favour of the grantee that is secured by the security interest. This result is a consequence of the fact that security is essentially a proprietary right. Consideration is not required to effect a pledge, or a

charge on property. While a security interest is a statutory creation, I see nothing in the *Personal Property Security Act*, R.S.O. 1990, c. P.10 (the "PPSA") that imposes a requirement for consideration as a condition of the effectiveness of a grant of a security interest.

[395] The Objecting Parties say that a requirement for consideration is found in the statutory provisions of the PPSA that require a security agreement between the parties. Given that any agreement requires consideration in favour of a party to the agreement to be enforceable against such party, the Objecting Parties say it necessarily follows that consideration is required for a party to enforce the grant of a security interest in its favour in a security agreement. I acknowledge that, in the absence of consideration, the other covenants in favour of a grantee of a security interest in a security agreement may not be enforceable. That is, however, a different issue. In such event, the rights of the grantee would be limited to its statutory rights under the PPSA, but the grant of the security interest would still be effective.

[396] Consistent with this approach, the PPSA expressly distinguishes between a security agreement and a security interest. A "security agreement" is defined in section 1(1) of the PPSA as "an agreement that creates or provides for a security interest and includes a document evidencing a security interest". I see no reason why a "document evidencing a security interest" cannot include a document or instrument containing a unilateral grant of a security interest by a grantor in favour of a grantee. Such a grant would be effective as between the parties regardless of whether consideration was given, provided the grantee could demonstrate that the grantor intended it to be delivered. It would also be effective in respect of the rights of third parties, subject to the other requirements of the PPSA regarding rights in the collateral and attachment. It is the extension of credit, and thereby the creation of an obligation in favour of the grantee that is secured by the security interest, that makes the security interest enforceable.

[397] Second, if consideration is required for the security interest granted in the October Security Agreement to be effective, I think this requirement was satisfied in three separate ways.

[398] First, the October Security Agreement recites that consideration was given, the receipt and sufficiency of which is acknowledged by both parties to the Agreement. It is an elementary principle that courts will not enter into an inquiry as to the adequacy of consideration: see John D. McCamus, *The Law of Contracts*, (Toronto: Irwin Law, 2005), at p. 222.

[399] Second, as a related matter, as stated above, the third recital to the October Security Agreement recites, in effect, that Credit Corp required the provision of security as a condition of continued advances under the Revolver Loan Agreement. This recital is consistent with the Court's conclusion above that an event of default had occurred under the Revolver Loan Agreement entitling Credit Corp to refuse to advance further monies under the Revolver Loan. On this basis, USS was therefore in a position to provide consideration in the form of a commitment to advance further funds under the Revolver Loan Agreement. Accordingly, the commitment to advance further funds on the part of Credit Corp referred to in the third recital accurately reflected the existence of consideration for the purposes of the October Security Agreement.

[400] Third, I am also of the opinion that any lack of consideration for the October Security Agreement was cured by the actual advances of monies under the Revolver Loan Agreement comprising the Second Tranche Indebtedness. If the execution of the October Security

Agreement and the advance of monies had occurred concurrently, there would have been no issue regarding a lack of consideration. The advance of monies itself would have satisfied any requirement for consideration under the October Security Agreement. In other words, under such circumstances, it would have been unreasonable, and unnecessary, to require demonstration of an intermediate commitment to advance further funds. The result should not change merely because there was a period of time between the execution of the October Security Agreement and the subsequent advance of monies under the Revolver Loan. The significance of the lapse of time is that the security interest was not enforceable, in the sense that the security interest did not secure any outstanding obligation and therefore could be enforced, until such time as an advance occurred under the Revolver Loan. It did not, however, render the October Security Agreement void for lack of consideration.

[401] The Objecting Parties raise three arguments to the effect that USS did not give any consideration, even if an event of default had arisen under the Revolver Loan Agreement which would otherwise have permitted USS to refuse to advance further funds under the Revolver Loan Agreement.

[402] First, the Objecting Parties say that, notwithstanding the occurrence of an event of default, USS had waived its right to assert such an event of default by advancing funds prior to January 2013. They say this course of conduct constituted a waiver of USS' right to assert such an event of default in October 2013 or of USS' right to use the event of default to deny further advances under the Revolver Loan at that time.

[403] This argument is rejected for three reasons. First, as a practical matter, the last advance which could have given rise to such a waiver took place in early January 2013. There is no evidence that USS knew that USSC was insolvent, and therefore that an event of default had occurred, at or prior to the time of any such advances. Second, as a legal matter, the language of the Revolver Loan Agreement excluded the operation of a waiver in October 2013 based on previous conduct on two grounds. The provisions of section 7 of the Revolver Loan Agreement require that, to be effective, any waiver must be in writing, which would exclude entirely the possibility of an unwritten waiver based on a course of conduct. In addition, section 7 expressly negates the operation of a waiver based on the granting of a previous waiver. Third, in any event, as a practical matter, there can be no doubt that, as between USS and USSC, USSC would have understood that no course of conduct by USS could have given rise to a waiver of USS' rights to determine the availability of funding under the Revolver Loan Agreement, as described above.

[404] Second, the Objecting Parties submit that USSC did not, in fact, provide consideration in the form of a commitment to advance further funds under the Revolver Loan. They base this argument on the fact that McQuade testified that he was never expressly advised by any USS representative that USS would refrain from advancing funds unless the October Security Agreement was signed. They also rely upon the fact that USS did not declare an event of default in October 2013.

[405] I do not accept this argument for the following reasons. By acceding to USS' position with full knowledge that USS was taking the position that it was entitled to withhold future advances, USSC must be taken to have accepted USS' legal position. In this regard, it is clear that McQuade understood that execution of the October Security Agreement was a condition of the further advance of funds to USSC at the time he signed the Third Revolver Amendment and

the October Security Agreement, notwithstanding the absence of any direct conversation on the matter with any USS representative. Further, McQuade's determination that execution of the October Security Agreement was in the best interests of USSC was expressly made on the basis of his understanding that USSC needed the advances to continue to meet its obligations and that USSC would only receive the further advances if it consented to the security.

[406] Accordingly, while McQuade says he believed that USS was obligated to fund under the Revolver Loan Agreement up to the limit of availability, he also knew that USS was taking the position that it was entitled to withhold funding under the Agreement until it received security for any further advances. McQuade did not challenge this legal position on behalf of USSC. Instead, USSC agreed to provide the security. In these circumstances, it was not necessary for USS to declare an event of default as a formal matter to assert its legal position. More importantly, in the absence of a determination at the time regarding the right of USS to withhold further advances, the decision of USSC to provide security must constitute acceptance of such legal right of USS.

[407] Lastly, the Objecting Parties say that, as a practical matter, USS was never going to stop advancing funds in October 2013 for reasons relating to the operational impact on USS and USSC as well as the potential triggering of cross-default provisions on the USS public debt. Whether or not this is true, I do not think it demonstrates an absence of legal consideration for the following reasons. First, the absence of a legal obligation to advance further funds is by itself sufficient to give rise to consideration. Second, the grant of security by USSC forecloses this argument as it become entirely speculative. The position of the Objecting Parties requires the Court to make a determination that, in the hypothetical situation in which USSC refused to provide the required security, USS would necessarily have advanced the monies comprising the Second Tranche Indebtedness. I do not think the Court could make such a determination on the limited evidence before it. Among other things, in order to make such a determination, the Court would need to address the other options that would have been available to USS in such circumstances, including a filing under the CCAA and DIP financing, which was raised at the time by the financial advisors to USS.Based on the foregoing, I do not accept the position of the Objecting Parties that the security constituted by the October Security Agreement is unenforceable for lack of consideration.

[408] For completeness, USS also argues that it gave consideration in the form of a forbearance from declaring a default, accelerating the Revolver Loan or instituting insolvency proceedings. These arguments also turn, at least in part, on the Court's acceptance of the contractual interpretation of the "unable to meet debts" event of default proposed in the Di Massa Report. Given the determination herein regarding consideration for the October Security Agreement, it is not necessary to address these potential additional sources of consideration, and I therefore decline to make a finding on these issues.

Alleged Fraudulent Preference

[409] In the alternative, if the October Security Agreement is held to be enforceable, the Objecting Parties submit that the Agreement constituted a fraudulent preference for the purpose of section 95(1)(b) of the BIA, as incorporated into the CCAA by the provisions of section 36.1 thereof. It is not disputed that the Objecting Parties bear the onus of proof in respect of this Objection.

[410] The provisions of section 95 of the BIA have been set out above. To succeed in this proceeding, the Objecting Parties must demonstrate: (1) a non-arm's length relationship between USSC and USS at the time of entering into the October Security Agreement; (2) that USSC was insolvent at the time of entering into the October Security Agreement; (3) that the October Security Agreement was entered into within twelve months of the Filing Date; and (4) that the October Security Agreement had the effect of giving USS, or more particularly Credit Corp as the lender under the Revolver Loan, a preference over other unsecured creditors at the date of delivery of October Security Agreement. There is no dispute that Credit Corp was not dealing at arm's length with USSC, that USSC was insolvent on and after October 30, 2013, and that the grant of security in favour of Credit Corp occurred less than one year prior to the Filing Date.

[411] USS argues, however, that the granting of security in the October Security Agreement did not give rise to a preference over another creditor entitling the Objecting Parties to relief under section 95 of the BIA. It bases this argument on the fact that the security in favour of Credit Corp is only being asserted in respect of advances made under the Revolver Loan after October 30, 2013, that is, in respect of the Second Tranche Indebtedness. USS bases its argument on the principle that there is no preference under section 95 if, and to the extent that, security is granted by a debtor company in respect of fresh advances which are used in the ongoing operations of the debtor company: see *McAsphault Industries Ltd. v. Six Paws Investments Ltd.*, [1995] O.J. No. 2450 (C.A.), at para. 19.

[412] The Objecting Parties make two submissions.

[413] The principal submission of the Objecting Parties is that the October Security Agreement constituted a fraudulent preference because Credit Corp obtained security in circumstances in which it was obligated to advance monies under the Revolver Loan Agreement. They say that, if Credit Corp had an unqualified obligation to advance monies under the Revolver Loan as and when requested by USSC up to such limit, delivery of the October Security Agreement would have constituted a fraudulent preference on the basis that delivery of security in such circumstances would be similar to providing security for past debts. This argument turns on the question of the extent to which Credit Corp was legally obligated to advance funds to USSC up to the limit of availability under the Revolver Loan Agreement as and when requested by USSC. It is a novel argument that could only arise, as a practical matter, in a non-arm's length situation.

[414] I have reservations regarding the merits of this argument as a matter of law. However, it is not necessary to determine the issue the alleged fraudulent preference on this basis. I have concluded above, in the context of the determination that USS provided consideration for the grant of the October Security Agreement, that Credit Corp was not obligated to advance further funds under the Revolver Loan Agreement. On this basis, this argument of the Objecting Parties cannot succeed.

[415] The alternative argument of the Objecting Parties is that the security in favour of Credit Corp under the October Security Agreement must fail in its entirety to the extent that the October Security Agreement purports to secure a pre-existing debt. They rely on *Re Fulton* (No. 2), [1926] O.J. No. 115 (C.A.), at para. 7, for this proposition.

[416] I accept that the granting of security for existing or past indebtedness constitutes a preference for the purpose of section 95 of the BIA. However, USS is not asserting a secured claim in respect of any such obligations in this proceeding, notwithstanding that the definition of "Secured Obligations" in the October Security Agreement extends to pre-existing indebtedness.

[417] In such circumstances, the Court of Appeal made it clear in *McAsphault*, at para. 19, that "a security may be bad in respect to some advances, but enforceable in respect to others, thus protecting payments made by an insolvent company which would otherwise be preferential." In that case, the evidence indicated that the fresh advances at issue were used in the on-going operations of the company. On that basis, the Court of Appeal held that the repayment of the advances did not constitute a fraudulent preference.

[418] In my opinion, the same principle operates in the present circumstances. There is no dispute that the advances comprising the Second Tranche Indebtedness were used in the on-going operations of USSC's business. The advances under the Revolver Loan after October 30, 2013 therefore benefitted the unsecured creditors as of the date of such advances. This factual context is sufficient under the case law to exclude a finding of a fraudulent preference under section 36.1 of the CCAA and section 95 of the BIA.

[419] The decision in *Fulton* does not assist the Objecting Parties for the reason that the circumstances in *Fulton* were qualitatively different from the present circumstances. *Fulton* involved advances under a chattel mortgage totaling $3,800, of which $2,200 represented a new advance after the date of the chattel mortgage. The mortgage purported to secure the existing obligation as well as the new advance. The security was declared invalid in respect of both advances. However, there was a significant issue with the new advance that explains the result in that decision. The Court of Appeal expressly held that there was "no doubt that the $2,200 did not in fact increase the assets of the estate in any tangible way." In fact, the court concluded that there was no evidence regarding what became of the $2,200. Accordingly, the security failed in its entirety because the new advance could not be demonstrated to have been used in the operations of the debtor, not because the mortgage also purported to secure a past advance.

[420] Based on the foregoing, I conclude that there is no basis for a finding that the delivery of the October Security Agreement constituted the grant of a fraudulent preference by USSC in favour of Credit Corp insofar as the security constituted thereby secured the Second Tranche Indebtedness.

Conclusion Regarding the Second Tranche Indebtedness

[421] Based on the foregoing, I conclude that Claim #11, being the claim in respect of the Second Tranche Indebtedness under the Revolver Loan, constitutes a debt claim, rather than an "equity claim", which is a Secured Claim for the purpose of this CCAA proceeding.

Remaining USS Secured Claims

[422] As mentioned, the Objecting Parties also submit that the security for the Remaining USS Claims (being Claims #11(a), 11(b) and 11(c)), should be invalidated on the grounds that the security for such Claims, being the November Security Agreement, is either unenforceable as a matter of contract law for lack of consideration at the time it was executed and delivered by USSC or void as constituting a fraudulent preference for the purposes of section 95(1)(b) of the

BIA. The Objecting Parties do not dispute the quantum of any of these three Claims nor do they suggest that these Claims are "equity claims". For completeness, the Objecting Parties also submitted that the November Security Agreement cannot be an enforceable obligation to the extent that the Court were to find that the October Security Agreement was unenforceable. Given the determination above, it is not necessary to address this submission.

[423] I propose to address the issues pertaining to the Remaining USS Secured Claims in the following order. First, I will describe the nature of the November Security Agreement. Then I will address the issues pertaining to Claim #11(c) (Intercompany Goods & Services), which relates to the provision of goods and services by USS to USSC prior to the Initial Order. Lastly, I will address the issues pertaining to Claim #11(a) (the Cliffs Transaction) and Claim #11(b) (Credit Support Payments), which involve different considerations, as these claims arose after the Filing Date.

The November Security Agreement

[424] On November 12, 2013, Credit Corp, USSC, USS, United States Steel International, Inc. and SHC executed a further amendment and restatement of the October Security Agreement that provided security to each of USS, United States Steel International, Inc. and SHC (collectively, the "USS Affiliates") in respect of the provision of intercompany goods and services on credit by any of them to USSC (as so amended, the "November Security Agreement") in addition to, and alongside, the security already provided to Credit Corp in respect of advances under the Revolver Loan pursuant to the October Security Agreement.

[425] The November Security Agreement contains recitals to the effect that each USS Affiliate sells "Goods" to USSC pursuant to arrangements and agreements, defined for such purposes as the "Sales Agreements", as between the USS Affiliates and USSC, that the USS Affiliates have determined that, in light of USSC's financial position and credit worthiness, they "no longer wish to sell Goods to the Debtor on terms other than cash in advance or cash on delivery, unless the Debtor provides acceptable financial accommodations" and that, "upon the Debtor's request, the [USS Affiliates] are willing to continue to sell Goods to the Debtor on credit…provided that the Debtor secures its obligations to pay for such Goods pursuant to the terms of the [November Security Agreement]". I would note that the definition of "Goods" for purposes of the November Security Agreement is "materials, goods and other products (including inventory and raw materials)".

[426] The extension of security to the USS Affiliates was implemented by adding the USS Affiliates as parties to the October Security Agreement, providing that such parties were "Secured Parties" for purposes of such Agreement, and amending the definition of "Secured Obligations" to read as follows:

> …all obligations, duties, indebtedness and liabilities of the Debtor from time to time owing by the Debtor to any Secured Party including, without limitation, obligations, duties, indebtedness and liabilities arising under, or in connection with: (i) the Loan Agreement; (ii) any amendment or restatement of the Loan Agreement, including any such amendment or restatement which increases or decreases the maximum amount of Loans and other obligations that may be made by Secured Party to Debtor thereunder; (iii) this Agreement; (iv) all obligations

> arising out of, in connection with or relating to the Sales Agreements or the sale of Goods by any USS Seller to the Debtor at any time and from time to time; and (v) any other document made, delivered or given in connection with any of the foregoing; in each case whether now existing or hereafter arising, whether evidenced by a note or other writing, whether allowed in any bankruptcy, insolvency, receivership or other similar proceedings, whether arising from an extension of credit, issuance of a letter of credit, acceptance, loan, guarantee, indemnification or otherwise, and whether direct or indirect, absolute or contingent, due or to become due, primary or secondary, or joint or several.

[427] By virtue of the definition of "Secured Obligations", therefore, all obligations owing by USSC to Credit Corp under the Revolver Loan Agreement, or to any of the USS Affiliates in respect of the sale of Goods, were entitled to the benefit of the general security interest granted by USSC in the Security Agreement, as amended and restated by the October Agreement and the November Security Agreement.

[428] I would also note that the first advance comprising the Second Tranche Indebtedness was made at the time that the October Security Agreement was in force and that the two later advances were apparently made after the November Security Agreement came into force. However, it is not disputed that the same security interest was continued under the November Security Agreement. I would also note that the parties addressed the validity of the security for the Second Tranche Indebtedness, and the existence of a fraudulent preference in respect of the granting of security for the Second Tranche Indebtedness, in the context of the October Security Agreement rather than the November Security Agreement. As the Objecting Parties have not raised any additional issues in respect of the Second Tranche Indebtedness pertaining to the November Security Agreement, I have proceeded on the basis that such Indebtedness is secured thereunder the extent that the security for the Second Tranche Indebtedness under the October Security Agreement is not invalidated for one of the reasons discussed above.

The Intercompany Trade Claim - Claim #11 (c)

[429] As mentioned, the Objecting Parties argue that the security for this Claim is either unenforceable for want of consideration from the USS Affiliates with respect to the November Security Agreement or void on the basis that the grant of the November Security Agreement constituted a fraudulent preference. I will address each issue in turn. I note that there is no issue regarding the fair market value of the goods and services relating to this Claim.

Alleged Unenforceability of the November Security Agreement

[430] The principles regarding the requirement for consideration in respect of the grant of a security interest in a security agreement have been addressed above in respect of the October Security Agreement. I do not propose to repeat that discussion in this section. As applied to the November Security Agreement, I reach the following conclusions.

[431] First, for the reasons set out above, I do not think that consideration is required for the grant of the security interest in the November Security Agreement.

[432] Further, to the extent that consideration is required to enforce the security constituted by the November Security Agreement, I find that consideration was given for the November

Security Agreement, as verified in the recitals in the Agreement and acknowledged by all the parties. In particular, the recitals to the November Security Agreement reflect the grant of consideration from the USS Affiliates in the form of a commitment to continue to provide the goods and services that are the subject of this Claim. The position of the USS Affiliates was made clear to McQuade before he executed the November Security Agreement on behalf of USSC. There is no evidence before the Court that would indicate that the USS Affiliates lacked the legal right to refuse to provide such goods and services if USSC had refused to provide the security. Insofar as the Objecting Parties suggest that the USS Affiliates were not going to stop providing these services, as a practical matter, I consider that the reasoning and conclusions reached in respect of the comparable argument made regarding the security for the Second Tranche Indebtedness is equally applicable in this context.

[433] In addition, any lack of consideration was cured by the delivery and provision by the USS Affiliates of the goods and services in respect of Claim #11(c). I note that such delivery is the substantive equivalent of an advance of funds to be used in the operations of USSC to acquire such goods and services. If USS had advanced the purchase price of such goods and services to USSC under the Revolver Loan for the purpose of payment of such obligations, such advances would have been secured pursuant to the October Security Agreement based on the conclusion reached above. There is no principled reason why the result would differ because the USS Affiliates provided goods and services rather than advanced funds for such purposes.

[434] Accordingly, I conclude that the November Security Agreement is not unenforceable in respect of the amounts constituting Claim #11(c) for lack of consideration from the USS Affiliates to USSC.

Alleged Fraudulent Preference

[435] The principles regarding the operation of section 95(1)(b) of the BIA have also been set out above. As discussed above, there is no evidence before the Court that the USS Affiliates were legally obligated to continue to provide the goods and services that are the basis for this Claim. The security constituted by the November Security Agreement was given in respect of a the provision of additional goods and services that would not otherwise have been provided to USSC. Accordingly, for the reasons set out above, I conclude that the grant of the security under by the November Security Agreement in favour of the USS Affiliates did not constitute a fraudulent preference in their favour for the purposes of section 95.

[436] Further, as stated above, the delivery and provision of the goods and services in respect of Claim #11(c) represents the substantive equivalent of a fresh advance of funds to USSC to be used in the operation of its business. On this basis, the grant of security in respect of the delivery and provision of such goods and services did not prejudice the unsecured creditors of USSC as of the date of delivery of the November Security Agreement or the date of the delivery or provision of such goods and services and does not constitute a fraudulent preference.

[437] Based on the foregoing, I conclude there is no basis for a finding that the delivery of the November Security Agreement by the USS Affiliates in respect of Claim #11(c) constituted the grant of a fraudulent preference by USSC in favour of such parties.

The Cliffs Transaction Claim and the Credit Support Payments Claim – Claims #11(a) and #(b)

[438] The claims for the Cliffs transaction and the credit support payments each arose after the Filing Date in the following circumstances.

[439] USSC took delivery from Cliffs of the iron ore that is the subject of the Cliffs transaction prior to the Filing Date. However, USS was not in a position to sell the iron ore to USSC until it had paid Cliffs. Because USS did not pay for the iron ore until after the Filing Date, its claim against USSC for payment of the iron ore arose after the Filing Date.

[440] USSC incurred the third-party obligations that are the basis of the credit support payments claim prior to the Filing Date but had not paid them as of that date. Because USS paid such claims pursuant to its guarantees in favour of such third parties after the Filing Date, its claim against USSC in respect of these payments also arose after the Filing Date.

[441] I will address each of these claims in turn.

The Cliffs Transaction – Claim #11(a)

[442] The Objecting Parties argue that the security for this Claim constituted by the November Security Agreement is either unenforceable or void as a fraudulent preference on the same grounds upon which they rely in respect of Claim #11(c). In addition, they argue that this claim is a pre-filing claim that is no different from all other trade creditor claims outstanding on the Filing Date. They argue that the effect of the November Security Agreement is to elevate improperly an unsecured pre-filing claim into a secured claim.

[443] This Claim involves the sale of goods by USS to USSC and is therefore similar as a factual matter to the circumstances in Claim #11(c). I conclude that the principles that governed the determinations with respect to Claim #11(c) regarding the issues of consideration for the November Security Agreement and the alleged fraudulent preference are equally applicable in the present situation, with the following additional consideration which reinforces the conclusions therein.

[444] In the case of this Claim, the Iron Ore Agreement specifically evidences fresh consideration for the grant of security pursuant to the November Security Agreement. While it is correct that USS was obligated to pay Cliffs under its agreement with Cliffs, as the Objecting Parties say, there is no evidence that USS was legally obligated to sell the iron ore to USSC once it acquired title to the ore. USS could have required that USSC deliver up possession of the iron ore to it. Instead, USS and USSC entered into a fresh agreement regarding the purchase by USSC of the iron ore at a time when USSC was independently represented. The Iron Ore Agreement provided that USSC's obligation to pay for such iron ore, when it arose, would be a "Secured Obligation" for purposes of the November Security Agreement, in return for USS' agreement effectively to sell USSC its interest in the iron ore and to pay Cliffs the purchase price of the ore on behalf of USSC.

[445] Such circumstances are sufficient to satisfy any requirement for the demonstration of consideration for the grant of security pursuant to the November Security Agreement in respect of the purchase price obligation of USSC and to negate any fraudulent preference upon the grant of such security for such obligation.

[446] I would add that, in the case of this claim, USSC expressly agreed to the secured treatment of the purchase price obligation prior to such obligation coming into existence. As such, the circumstances do not involve the transformation of a pre-filing unsecured claim into a post-filing secured claim.

The Credit Support Payments Claim – Claim #11(b)

[447] As discussed above, USS paid these obligations pursuant to guarantees established in favour of the third-party creditors. It asserts Claim #11(b) against USSC pursuant to its rights of subrogation. USS submits that such rights of subrogation constitute "Secured Obligations" for the purposes of the November Security Agreement and, accordingly, rank ahead of all other trade creditors. If these credit support payments are secured, a consequence would be that the unsecured, pre-filing claims of the third party-creditors have become secured, post-filing claims of USS without any involvement of the Monitor or the Court pursuant to the provisions of section 10 of the Initial Order, which would otherwise govern the payment of pre-filing obligations.

[448] The Objecting Parties argue that the security for this Claim constituted by the November Security Agreement is either unenforceable or void as a fraudulent preference on the same grounds upon which they rely in respect of Claims #11(a) and #11(c).

[449] After a review of the documentation pertaining to this Claim, I think there is a threshold issue of whether the USS subrogation rights at issue qualify as "Secured Obligations" under the November Security Agreement. This issue was not, however, raised directly in the submissions of the parties. The parties should therefore be given an opportunity to make submissions regarding this threshold issue to the extent they wish to do so.

[450] Accordingly, I do not propose to address the determination of the issues pertaining to this Claim at this time. If the parties are unable to agree on a schedule for submissions on the threshold issue, they should contact the Court to arrange a telephone case conference at their convenience.

Conclusions

[451] he USS Claims referenced as Claims #1-8 inclusive in the Monitor's Third Report are not disputed in this proceeding and are therefore confirmed as unsecured Claims under the Claims Process Order. Based on the foregoing, the USS Claims referenced in such Report as Claims #9 and #10 are also confirmed as unsecured Claims under the Claims Process Order and Claims #11, #11(a) and #11(c) are confirmed as Secured Claims. The USS Claim referenced in the Report as Claim #11(b) remains to be determined.

Wilton-Siegel J.

Date: February 29, 2016

TAB 20

Ontario Supreme Court
Wiebe, Re
Date: 1995-02-06

Re bankruptcy of Peter Victor Wiebe

Ontario Court of Justice (General Division) [In Bankruptcy] Kozak J.

Judgment – February 6, 1995.

(Doc. 48-94B)

[1] February 6, 1995. KOZAK J.: – This is an application pursuant to R. 94 of the *Bankruptcy Act* for a determination as to whether the contingent claim of the Thunder Bay District Health Unit is a provable claim and, if so, the value of the said claim.

Factual Background

[2] The bankrupt, Peter Victor Wiebe, is a dentist who is licensed and duly qualified to carry on a private practice in the Province of Ontario. An assignment in bankruptcy was filed on his behalf on November 5, 1993. On November 25, 1993, a proof of claim was filed by the Thunder Bay District Health Unit in which the sum of $94,458.58 was shown as an unsecured debt owing by the bankrupt to the said creditor. The amount shown as being owing arises out of an agreement, in writing, dated January 2, 1992 under which the Thunder Bay District Health Unit advanced to Doctor Wiebe the sum of $94,458.58 for the purpose of becoming qualified as a Dental Director in Public Health so that the Health Unit could hire him as its Dental Director. In this regard I take it that Doctor Wiebe successfully completed the necessary courses to qualify himself to practice as a Dental Director in Dental Public Health in the Province of Ontario, and that he commenced employment with the Health Unit in that capacity on September 1, 1993. The affidavit material filed indicates that he continues to be so employed.

[3] Paragraph 5 of the agreement between Doctor Wiebe and the Health Unit states:

> Provided the Dentist successfully obtains the necessary qualifications and is employed by the Health Unit for the period September 1, 1993 to February 28, 1998 as its Dental Director then all monies loaned to him or paid on his behalf by the Health Unit shall be forgiven.

On the other hand, para. 3(d) states:

> Except in the occurrence of death or permanent disability in the event that the Dentist enters employment with the Health Unit but his employment is terminated before completing the required period of service of 54 months commencing September 1, 1993 to February 28, 1998 of such service, then all monies advanced to the Dentist or on his behalf pursuant to paragraph 2 shall forthwith be due and payable on demand by him to the Health Unit together with interest at the rate of 11 percent per annum calculated from the dates of the respective advances or payments on his behalf.

[4] On August 5, 1994 a discharge hearing took place at which time the bankrupt's discharge was ordered suspended for a period of four months and he was discharged on December 5, 1994. Subsequent to the discharge the trustee came into possession of an unexpected sum in the amount of $2,500 and now wishes to have this amount paid out to the unsecured creditors. Hence the need to have the contingent claim of the Thunder Bay Health Unit determined as a provable claim and valued.

Legal Considerations

[5] Section 121(1) makes it clear that only debts to which the debtor is liable before the date of the bankruptcy or those to which he may become subject before his discharge, by reason of an obligation incurred before the bankruptcy, share in the assets vested in the trustee.

[6] Rule 94(1) provides that when a contingent or unliquidated claim is filed with the trustee, he shall, unless he compromises the claim, apply to the Court to determine whether the claim is a provable claim and, if so, to value the claim.

[7] A provable claim must be one recoverable by legal process (*Farm Credit Corp. v. Holowach (Trustee of)* (1988), 68 C.B.R. (N.S.) 255 (Alta. C.A.)). To be a provable claim under s. 121(2), a claim must not be too remote and speculative. To establish that a contingent claim or unliquidated claim is a provable claim, a creditor must prove more than he has been sued, and that he has an indemnity agreement from the bankrupt. There has to be an element of probability of liability arising from the Court proceedings. If there are too many ifs about the action and the applicability of the indemnity agreement before a provable claim comes into being, the claim is not a provable claim under s. 121(2). See *Claude Resources Inc. (Trustee of) v. Dutton* (1993), 22 C.B.R. (3d) 56 (Sask. Q.B.).

Decision

[8] This is a case where the bankrupt has now been employed as the Dental Director of the Health Unit since September 1, 1993 and it

would appear that he is performing his job function in a satisfactory manner. According to the Trustee, there is no present intention, on the part of the bankrupt, to leave his current employment, nor is there any indication at the present time, on behalf of the Health Unit, to terminate the employment of the bankrupt. The parties are content with the present arrangement which has existed for the past 18 months, and it is anticipated that the status will prevail until February 28, 1998 at which time the loan to the bankrupt will be forgiven. And yet, the contingency that the bankrupt might leave his employment or be terminated by his employer prior to February 28, 1998 and thereby incur liability for the loan is not so speculative or remote a probability as to render the creditor's claim unprovable. There are any number of reasons as to why a person might leave a position such as this or be terminated for cause. The bankrupt might receive a better job offer, wish to return to private practice, or move to another area. On the other hand, there might be misconduct or misbehaviour on the part of the bankrupt in the performance of his duties that could result in his dismissal prior to the expiration of the 54 month period. There is a case to be made for the Court to consider some factor for the happening of the contingency in this case. Accordingly, it is the finding of this Court that the creditor, Thunder Bay District Health Unit, has proven its claim.

[9] As to the value of the said claim, the Court must look to what is reasonable in the circumstances. Given the current state of satisfaction of the parties, the tenure of the bankrupt on the job and the period remaining in the agreement, this Court values the claim at approximately ten percent of its face value which would be $9,500.

Order accordingly.

TAB 21

CITATION: YG Limited Partnership and YSL Residences Inc. (Re), 2024 ONSC 1617
COURT FILE NO.: BK-21-02734090-0031
DATE: 20240319

SUPERIOR COURT OF JUSTICE – ONTARIO (COMMERCIAL LIST)

RE: IN THE MATTER OF THE BANKRUPTCY AND INSOLVENCY ACT, R.S.C. 1985, c. B-3, as amended

IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF YG LIMITED PARTNERSHIP AND YSL RESIDENCES INC. OF THE CITY OF TORONTO, IN THE PROVINCE OF ONTARIO

BEFORE: KIMMEL J.

COUNSEL: *Mark Dunn and Brittni Tee,* Lawyers for the Appellant, Maria Athanasoulis

Matthew Milne-Smith and Chenyang Li, Lawyers for the Proposal Trustee, KSV Restructuring Inc.

Shaun Laubman, Lawyers for 2504670 Canada Inc., 8451761 Canada Inc. and Chi Long Inc.

Alexander Soutter, Lawyers for 2576725 Ontario Inc., Yonge SL Investment Limited Partnership, 2124093 Ontario Inc., E&B Investment Corporation, SixOne Investment Ltd., Taihe International Group Inc.

HEARD: December 18 and 22, 2023

ENDORSEMENT
(APPEAL FROM DISALLOWANCE OF CLAIM)

The Appeal

[1] The debtor YSL Residences Inc. ("YSL") owned a development property (upon which it was intended that an 85-story retail and condominium complex in downtown Toronto would be built in two stages, the "YSL Project"). YSL was the general partner and held the YSL Project as bare trustee for the YG Limited Partnership ("YG"). Maria Athanasoulis was employed by YSL and the Cresford group of companies, owned and controlled by Daniel Casey and his family members (the "Cresford Group").

[2] YSL and YG filed a Proposal under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "BIA") and were deemed bankrupt on April 21, 2021. The Proposal Trustee, KSV Restructuring Inc. ("Proposal Trustee"), was appointed in the context of the Proposal proceedings.

[3] Maria Athanasoulis filed a proof of claim against YSL for two unsecured claims (together, the "Athanasoulis Claim"):

a. $1 million in respect of damages for wrongful (constructive) dismissal (the "Wrongful Dismissal Claim"); and

b. $18 million in respect of damages for breach of an oral agreement that Ms. Athanasoulis would be paid 20 percent of the profits earned on the YSL Project (the "Profit Share Claim").

[4] In accordance with the established claims procedure,

a. On March 30, 2023, the Proposal Trustee delivered to Ms. Athanasoulis notice that it would accept her Wrongful Dismissal Claim in the amount of $880,000.39.

b. On August 10, 2023, the Proposal Trustee delivered to Ms. Athanasoulis a Notice of Disallowance of her $18 million Profit Share Claim (the "Disallowance").

[5] The Proposal Trustee's partial allowance of the Wrongful Dismissal Claim has not been challenged. This is an appeal (by way of motion under the BIA) from the Proposal Trustee's Disallowance in full of Ms. Athanasoulis' $18 million Profit Share Claim.

[6] Ms. Athanasoulis moves for an order setting aside the Disallowance of her Profit Share Claim and directing a reference to quantify the value of her damages, and ancillary relief with respect to the validity, value and priority of that claim, among other relief. The Disallowance is ordered to be set aside and certain of the other requested relief is granted (as detailed at the end of this endorsement), for the reasons that follow.

The Proposal Proceedings

[7] YG and YSL (together in the context of these proceedings referred to as "YSL" or the "Debtor") filed Notices of Intention to Make a Proposal under the BIA, which were procedurally consolidated pursuant to an Order dated May 14, 2021. The original filing and deemed date of bankruptcy was on April 30, 2021.

[8] An Amended Third Proposal dated July 15, 2021 (the "Proposal") was supported by the unsecured creditors of the Debtors and approved by this court on July 16, 2021. Under the Proposal, the Proposal Trustee was authorized to deal with various claims against the Debtor, some of which (such as the Athanasoulis Claim) were disputed.

[9] The Proposal provided that Concord Properties Developments Corp. (the "Sponsor") would acquire the YSL Project in exchange for three principal forms of consideration: (i) the Sponsor would assume 100% liability for of all secured creditor claims and construction lien claims; (ii) the Sponsor would pay to the Proposal Trustee a pool of cash of $30.9 million to be distributed to unsecured creditors with proven claims; and (iii) any residual amounts left unclaimed from the cash pool to be distributed to equity stakeholders through the limited partners or as they may direct in accordance with the limited partnership agreements.

[10] These equity stakeholders include the Class A limited partners (unitholders) of the YG Limited Partnership (the "LPs"). The LPs include 2504670 Canada Inc., 8451761 Canada Inc. and Chi Long Inc. (collectively sometimes referred to as the "250 LPs"), and 2576725 Ontario Inc., Yonge SL Investment Limited Partnership, 2124093 Ontario Inc., E&B Investment Corporation, SixOne Investment Ltd., and Taihe International Group Inc. The LPs collectively advanced $14.8 million to the Debtors in exchange for Class A Preferred units in YG Limited Partnership.

[11] The Athanasoulis Claim is an unsecured claim that, if proven, would be funded from the $30.9 million pool of cash that has been set aside to satisfy proven unsecured creditor claims.

[12] Dunphy J. made the following findings (in *YG Limited Partnership and YSL Residences (Re)*, 2021 ONSC 5206, 93 C.B.R. (6th) 139) at the time the Proposal was approved:

a. Whatever questions there may be regarding the solvency of the debtors from the perspective of the realizable value of their assets, there can be no question of the insolvency of the debtors from a liquidity point of view: secured and unsecured claims alike are overdue and unpaid and the debtors have no means to satisfy their claims in a timely way. Lien claims are more than a year in arrears for the most part while all forbearance periods have expired for the secured debt (para. 17).

b. The Proposal does not answer the question of what the value of the project might have been had the project been offered on the open market in a competitive process (para. 21).

c. This project is, at its core, a hard asset consisting of real estate, a bundle of approvals and a hole in the ground. There is no goodwill to speak of. It has been held in limbo for much more than a year (para. 33(a)).

[13] Dunphy J. made certain findings in his decision not to approve an earlier proposal put forward by the Debtors, in *YG Limited Partnership and YSL Residences (Re)*, 2021 ONSC 4178, 93 C.B.R. (6th) 109 as follows:

a. Few things are more precious in the restructuring business than time. YG LP was able to "purchase" more than a year of time with the forbearance arrangements that it worked out. That precious time appears to have been devoted solely to finding transactions that offered the greatest level of benefits for the Cresford group of companies (para. 76).

b. There was a window of time to find an out-of-court solution, but it would appear that the debtors have squandered it (para. 82).

The Arbitration

[14] The Proposal Trustee and Ms. Athanasoulis agreed to submit the Athanasoulis Claim to arbitration. The arbitration was to proceed in two stages. The first stage proceeded and Arbitrator William Horton issued an initial award on March 22, 2022 (the "Arbitral Award") in which he held that an oral Profit Sharing Agreement had been entered into as a term of Ms. Athanasoulis' employment (the "Profit Sharing Agreement") entitling her to 20% of the profits earned on all

current and future Cresford projects, including the YSL Project.[1] This Profit Sharing Agreement was expected to represent fair compensation for her existing and expected future contributions to the profitability of the projects.

[15] Arbitrator Horton found that the Profit Sharing Agreement was not a standalone agreement. It was an existing part of an integral contract of employment that had been acted on by both sides for fifteen years as Ms. Athanasoulis worked her way up through the ranks of the Cresford Group.

[16] The Arbitrator found the key terms of the Profit Sharing Agreement as they pertain to the YSL Project to be the following:

a. Profits were to be calculated, on a good faith basis, based on the pro forma budgets prepared by Cresford using revenues less expenses for each project (updated from time to time as expenses were incurred and circumstances evolved). It was understood that the realized profits for each project would ultimately have to be accounted for with third party investors.

b. Profits could not be artificially reduced by "bad faith" transactions.

c. It was expected to take several years (possibility 5–7 years) in the normal course to complete a project like the YSL Project. This implied a mutual commitment on both sides.

d. Ms. Athanasoulis' profit-share interest was to be paid by YSL.

e. The Profit Share was to be paid to Ms. Athanasoulis when profits were earned, usually at the completion of a project.

f. There was no requirement that Ms. Athanasoulis remain employed at the time that a profit was earned.

[17] Arbitrator Horton made certain findings about Ms. Athanasoulis' employment history with the Cresford Group. She began working at the Cresford Group in 2004 as a Manager, Special Projects. She had limited prior education or experience. By 2013 she had worked her way up to one of the two senior officer positions reporting directly to the founder, president and sole director, Daniel Casey. She served as an officer of various companies in the Cresford Group and was the Vice President and Secretary of YSL.

[1] The Arbitrator found that there had been an earlier profit sharing agreement dating back to 2014 to pay Ms. Athanasoulis an agreed upon 10% of the profits from a successfully completed project that was then expanded to cover other future projects and eventually increased to 20%.

[18] Arbitrator Horton found that Ms. Athanasoulis was constructively dismissed by YSL in December 2019. She was, at the time of her termination in December 2019, the President and COO of the Cresford Group, and an employee and officer of YSL.

[19] The Proposal Trustee and Ms. Athanasoulis agree that they are bound by the findings made by the Arbitrator in the Arbitral Award.

[20] In her testimony during the Arbitration, Ms. Athanasoulis testified in response to questions about the terms of the oral Profit Sharing Agreement and specifically about how the profit would be calculated under that agreement: "it would be calculated after paying the [specific project] costs and after the equity was repaid to the LP investors."

[21] In the second stage of the Arbitration, the Proposal Trustee and Ms. Athanasoulis had intended (and agreed) that the Arbitrator would determine any damages payable arising out of his findings in the first stage (as reflected in the Arbitral Award) regarding the Profit Sharing Agreement and Ms. Athanasoulis' constructive dismissal, corresponding with her Profit Share Claim and her Wrongful Dismissal Claim.

[22] However, after the first stage Arbitral Award was released, as a consequence of opposition raised by the LPs and the Sponsor (who had not been privy to the original submission to arbitration), this court ordered in the Funding Decision (described below) that the second phase of the Arbitration would not proceed. Instead, the court directed the Proposal Trustee to determine the Athanasoulis Claim. It is the Proposal Trustee's initial determination, and Disallowance, of the Profit Share Claim that is the subject of this appeal.

The Funding Decision: Directions for the Proposal Trustee to Determine the Athanasoulis Claim

[23] The Sponsor's obligation to fund administrative fees and expenses incurred by the Proposal Trustee in connection with the resolution of the Athanasoulis Claim was determined in a November 1, 2022 endorsement: *YG Limited Partnership (Re)*, 2022 ONSC 6138, 5 C.B.R. (7th) 389 (the "Funding Decision").

[24] The Funding Decision determined that the Sponsor was not obligated to fund phase two of the arbitration in which Ms. Athanasoulis and the Proposal Trustee had agreed to participate. That conclusion was reached on the basis that phase two of the proposed arbitration improperly delegated to the Arbitrator the responsibility of determining the Athanasoulis Claim. Neither the Sponsor nor the LPs had been privy to the submission to Arbitration. For different reasons, they each objected to the Arbitration proceeding to phase two.

[25] The Funding Decision directed the Proposal Trustee to determine and value the Athanasoulis Claim in a timely and principled manner based on the findings in the Arbitral Award and building on them. Upon the request of the Proposal Trustee, the court provided advice and directions concerning the process for determining of the Athanasoulis Profit Share Claim and any appeal therefrom (the "Claim Procedure"). See *YG Limited Partnership (Re)*, 2023 ONSC 4638 (the "Claims Procedure Endorsement").

[26] The LPs were granted standing to participate in the Claim Procedure for the determination of the Profit Sharing Claim and any appeal thereof, subject to the discretion and further direction of the appeal judge. The rationale and terms for the standing granted to the LPs is described at paragraphs 55 and 56 of the Claims Procedure Endorsement:

> [55] Here, the LPs have been afforded standing to provide evidence and make submissions to the Proposal Trustee in connection with the Notice of Determination regarding the "provability" of the Profit Share Claim. They have a unique perspective to offer with respect to their argument that the Profit Share Agreement should be found to be unenforceable because it is contrary to the Limited Partnership Agreement (a ground not relied upon by the Proposal Trustee but raised and therefore forms part of the record for appeal purposes that Ms. Athanasoulis must respond to).
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> [56] The LPs may also have a unique perspective on the preliminary question of whether the Profit Share Agreement can be enforced in the face of Ms. Athanasoulis' admissions that she agreed with the LPs that they would be paid out before her. These unique perspectives have been placed before the Proposal Trustee; Ms. Athanasoulis will be permitted to respond to and challenge them, and they will be "in play" on any appeal.

[27] The Proposal Trustee had indicated that there were threshold issues that it wished to raise that did not involve an in-depth valuation of the Profit Share Claim and that might be dispositive. The parties agreed that they should not be required to go to the expense of fully briefing the valuation issues, with experts if deemed appropriate, until those threshold issues had been considered.

[28] That is how the Proposal Trustee has proceeded, leading to its Disallowance of the Profit Share Claim. The Claims Procedure Endorsement (at paras. 44 and 63) indicated that it was not expected that there would be any material or submissions at this time regarding the future oriented (or "but-for") damages, whether calculated at the repudiation date or the date of bankruptcy. If Ms. Athanasoulis is successful on her appeal of any disallowance of the Profit Share Claim, the Claims Procedure Endorsement directs the parties to make an appointment for a case conference to seek directions about the process for the determination of the more complex valuation questions that may require expert input.

The Grounds for the Disallowance and Grounds of Appeal

[29] Following the Funding Decision and the Claims Procedure Endorsement, and the implementation of the procedures contemplated thereby, the Proposal Trustee issued its Notice of Disallowance in respect of the Athanasoulis Claim. The Proposal Trustee's stated grounds in the Notice of Disallowance for disallowing the Profit Share Claim were that:

a. It is not a debt obligation or liability of YSL but rather, in substance, an equity claim, that is not a provable claim under the BIA.

b. There was no profit to be shared, because none had been earned by YSL as of the date of either the termination of Ms. Athanasoulis' employment (December 2019) or the date of bankruptcy (April 2021). Ms. Athanasoulis cannot claim a share of a non-existent profit.

c. Further, to the extent it is based upon projected future profitability, it is a contingent claim for a lost profit share that is far too remote to be capable of being considered a provable claim. Nor can it be the subject of any meaningful and reasonable computation, and it is thus valued at zero.

d. It is subordinated to the LPs' entitlements because she was only to receive her share of the profits when Cresford did, which would occur only after the LPs had been repaid their capital and earned their entire preferred return. The LPs have not, and due to lack of available funds will not, receive all such amounts.

[30] The following errors are identified in Ms. Athanasoulis' September 8, 2023 Notice of Motion appealing from the Trustee's Disallowance of her Profit Share Claim:

a. The Trustee erred in its conclusion that the Profit Share Claim is not a claim provable in bankruptcy, having erroneously characterized it as:

   i. "in substance" an "equity claim" without regard to the statutory definition of an "equity claim" in the BIA, which provides that an equity claim can exist if, and only if, it is "in relation to" an "equity interest";

   ii. a contingent claim that is too speculative or remote.

   (Collectively, the "Provable Claim Errors")

b. The Trustee erred in valuing the Profit Share Claim at zero:

   i. based on the erroneous assumption that Ms. Athanasoulis is only entitled to 20% of the actual profits earned by YSL or that YSL is capable of earning, taking into consideration its subsequent insolvency, whereas damages for breach of contract must put the injured party in the position she would be in if the other party had met its contractual obligations, calculated at the time of the breach or repudiation of the contract without regard to subsequent events;

   ii. without even attempting to calculate either YSL's revenues or expenses to determine its profits earned on the relevant date (of repudiation), despite the existence of contemporaneous evidence about the prospect of a sale of the YSL Project or YSL's contemporaneous pro forma projections that indicated YSL's expectation of profits at that time.

   (Collectively, the "Claim Valuation Errors")

c. The Trustee erred in concluding that Ms. Athanasoulis is not entitled to be paid anything unless and until the LPs are paid in full, thereby subordinating her Profit Share Claim to the LPs equity claims.

(The "Subordination Error")

[31] The alleged errors addressed in the written and oral submissions made on behalf of Ms. Athanasoulis on the appeal generally fall within the originally identified above three categories of errors identified in the Notice of Motion on appeal. These core errors are focused on the extricable errors of law that were identified during oral submissions and subject to review on the standard of correctness. To the extent that they depend upon mixed errors of fact and law, Ms. Athanasoulis argues that they reflect unreasonable findings and palpable and overriding errors that warrant this court's intervention.

Economic/Financial Implications

[32] The available pool of funds set aside upon the sale to the Sponsor under the approved Proposal will be paid first to satisfy accepted claims of all unsecured creditors with proven claims and then the remaining balance will be paid to the LPs. The total amount of other unsecured claims is not yet known, but the Proposal Trustee does not expect them to come close to the available $30.9 million in the pool. The estimate at the time of this appeal was that the total of other unsecured claims that the Trustee has accepted add up to approximately $14.9 million. However, even if the Profit Share Claim is not allowed (or valued at or close to zero) and the LPs receive the balance of the pool of available funds, it is not expected to cover the full amount of their claims.

[33] If Ms. Athanasoulis is found to have a provable claim, the available pool of funds will be distributed *pro rata* to her (based on the value of her claim once determined) and to the other unsecured creditors whose claims have been allowed. If the Profit Share Claim is allowed and is valued at or close to what has been claimed, the other unsecured creditors will receive something (although possibly not the full amount of their allowed claims) but it is not expected that the LPs will be repaid any of their investments in this scenario.

[34] The "either or" scenario comes down to the competing claims of the LPs and Ms. Athanasoulis if her Profit Share Claim is allowed and is valued as she suggests. However, there are variables in the valuation of the Profit Share Claim that could lead to amounts being paid to both, for example under the alternative valuation scenario that Ms. Athanasoulis proposes of $7.8 million the unsecured creditors (including Ms. Athanasoulis) and the LPs may all receive something from the pool.

The Standard of Review

[35] The parties agree that is a "true appeal" of the Proposal Trustee's determination.

[36] Although a reasonableness standard of review was suggested by both Ms. Athanasoulis and the Proposal Trustee as one that may apply in Ontario, I have concluded that the appropriate standard of review is palpable and overriding error absent an extricable question of law, which is reviewable on a correctness standard. See *8640025 Canada Inc. (Re)*, 2018 BCCA 93, 8 B.C.L.R. (6th) 225 at para. 65. See also *Re Casimir Capital*, 2015 ONSC 2819, 25 C.B.R. (6th) 149, at para.

33 regarding the standard of review for extricable errors of law. Ms. Athanasoulis has the onus of demonstrating such errors.

[37] Earlier cases dealing with the standard of review of a decision of a trustee disallowing a claim under the BIA on a reasonableness standard (including cases in Ontario, such as *Re Charlestown Residential School*, 2010 ONSC 4099, 70 C.B.R. (5th) 13, at para. 17) followed the earlier case of the British Columbia Court of Appeal, in *Galaxy Sports Inc. (Re)*, 2004 BCCA 284, 29 B.C.L.R. (4th) 362, at paras. 39 and 43. It was brought to the court's attention in the course of the full briefing on this appeal that the line of reasoning emanating from *Galaxy Sports* has been superceded by the later decision of the same (BC) Court of Appeal in *864*.

[38] While the decision in *864* deals specifically with appeals from decisions of claims officers under the *Companies' Creditors Arrangement Act* ("CCAA"), applying the same standard of review to appeals brought in respect of determinations of claims made pursuant to s. 135(4) of the BIA would accord with the Supreme Court of Canada's directive that CCAA and BIA proceedings should be treated as one "integrated body of insolvency law". See *Century Services Inc. v. Canada (Attorney General)*, 2010 SCC 60 at paras. 76–78.

[39] The Ontario Court of Appeal has made reference to the standard of review of determinations of BIA claims applied in *Galaxy Sports*, but also observed that "reasonableness" standard has not been explicitly adopted in Ontario. See, for example, *Credifinance Securities Limited v. DSLC Capital Corp.*, 2011 ONCA 160, 277 O.A.C. 377, at paras. 24–27). The Supreme Court's decision in *Canada v. Vavilov*, 2019 SCC 65, [2019] 4 S.C.R. 653 which held that statutory appeals from administrative decision makers are subject to the ordinary appellate review standard as opposed to a reasonableness standard, supports the evolved reasoning of the British Columbia Court of Appeal in the more recent decision in *864*.

[40] Ms. Athanasoulis contends that there are errors of law underpinning all of the grounds of appeal, which are reviewable on the standard of correctness. Ms. Athanasoulis further contends that to the extent any errors are not found to be reviewable on the correctness standard because they are dependent upon factual determinations or the application of the law to the facts, those errors fail under both the reasonableness and the palpable and overriding error standards.

[41] The following analysis applies the standard used in *864* of palpable and overriding error to any of the identified errors not found to be extricable errors of law (which are reviewed applying the standard of correctness). However, the outcome would have been the same if the errors not subject to the correctness standard had been reviewed on the reasonableness standard.

Summary of Outcome

[42] Ultimately, while the court does so cautiously and only sparingly, I have concluded that the grounds for the Disallowance are predicated upon a fundamental and extricable error in the mischaracterization of the nature of the Profit Share Claim as an equity claim contingent upon existing or future profits that have not been, and will now never be, realized. This mischaracterization of the Profit Share Claim has led to further compounding errors, in that the Disallowance also failed to properly consider and assess the type of loss that the Profit Share Claim seeks to recover, which is in damages for breach of contract that crystalized when Ms.

Athanasoulis was constructively dismissed in December 2019 (once she accepted the repudiation and sued for damages).

[43] As a result of these mischaracterizations of the nature of the Profit Share Claim and the type of loss that it entails, the Proposal Trustee did not to attempt to value it. That is the valuation exercise that the Claims Procedure Decision contemplated might be required if the threshold "provability" determinations were found to be in error, which they have been.

[44] The Profit Share Claim must now be valued, even if it might be difficult to do so and might depend upon expert inputs to quantify her damages. It is not guaranteed that the result of that process will be that its value is established at, or even near, the levels that Ms. Athanasoulis has claimed; however, that exercise cannot be avoided by the Proposal Trustee's threshold determinations that were predicated upon fundamental mischaracterizations of the nature of the Profit Share Claim and the appropriate timing and measure of the loss.

[45] The court understands why the Proposal Trustee proposed to proceed in the manner it did, by its initial determination of the Profit Share Claim based on somewhat complex threshold "provability" considerations that might have saved considerable time and expense had the Proposal Trustee's characterizations been correct in law. However, they were not. The Profit Share Claim is significant, and its ultimate determination has implications for other creditors (not just the LPs). Thus, the further time and effort to determine this claim will need to be invested by the Proposal Trustee.

[46] The court also understands why the Proposal Trustee and Ms. Athanasoulis originally agreed to arbitrate the Athanasoulis Claims given the complexity of the issues underlying the necessary determinations. However, that is water under the bridge in light of the objections raised by the Sponsor and the LPs in conjunction with the Funding Decision (and the later Process Decision). Whether this procedure of having the Proposal Trustee do its best to determine and value the Athanasoulis Claims and then have the court review those determinations on appeal proves to be less expensive remains to be seen, but, absent further agreement, this is the process that the parties are now engaged in. It is more transparent for the stakeholders.

Analysis: Allege Errors of the Proposal Trustee in the Notice of Disallowance

[47] Each of the categories of errors alleged by Ms. Athanasoulis to have been made by the Proposal Trustee will be addressed in turn, followed by a discussion of the additional points raised by the LPs that do not come directly within the parameters of the alleged errors.

A) The Provable Claim Errors

[48] Did the Proposal Trustee err in its conclusion that the Profit Share Claim is not a claim provable in bankruptcy, on the basis that:

a. it is "in substance" an "equity claim"; and/or

b. it is a contingent unliquidated claim that is too speculative or remote.

[49] A "provable claim" is defined in s. 121(1) of the BIA, which provides: "All debts and liabilities, present or future, to which the bankrupt is subject on the day on which the bankrupt becomes bankrupt ... shall be deemed to be claims provable in proceedings under this Act."

[50] Sections 121(2) and 135(1.1) or the BIA require the Proposal Trustee to determine whether any contingent claim or unliquidated claim is a provable claim, and, if it is a provable claim, to value it.

Equity Claim

[51] An equity claim is not a debt or liability and is not a provable claim under the BIA.

[52] An "equity claim" is defined in s. 2 of the BIA to be a claim "that is in respect of an equity interest." Section 2 of the BIA states that an equity interest means "a share in the corporation, or warrant or option or another right to acquire a share in the corporation...".

[53] When a word or phrase is defined with reference to what it "means" that has been held to signal that this definition is intended to be exhaustive, in accordance with well-accepted principles of statutory interpretation. See *Entertainment Software Association v. Society of Composers, Authors and Music Publishers of Canada*, 2012 SCC 34, [2012] 2 S.C.R. 231, at para. 42; *Alexander College Corp. v. R.*, 2016 FCA 269, 410 D.L.R. (4th) 299, at para 14.

[54] The definition of "equity claim" in s. 2 goes on to provide, by way of example, a non-exhaustive list of types of equity claims, including a claim for a dividend, return of capital, redemption or retraction, monetary loss resulting from the ownership, purchase or sale of an equity interest, or a claim for contribution or indemnity in respect of these other types of claims. However, all of these examples are tied to the originally essential component of the definition that it be "a claim that is in respect of an equity interest", meaning a share (or warrant or option to acquire a share).

[55] The Trustee asserts in its Notice of Disallowance that it "does not consider it relevant that Ms. Athanasoulis does not hold equity in YSL". Its position on this appeal is that the Profit Share Claim is "in substance" an equity claim. It argues that since the Profit Share Claim is derivative of the residual "profit" or equity that would be left for the owners (the Class B Unitholders) it is a claim inextricably linked to and therefore in respect of an ownership interest even if not itself an ownership interest.

[56] The Proposal Trustee relies on the Ontario Court of Appeal's decision in *Sino-Forest Corporation (Re)*, 2012 ONCA 816, 114 O.R. (3d) 304, at para. 44, which states that the term equity interest should be given an expansive meaning. In that case, the claim by the auditors for contribution and indemnity was derivative of a claim against them by corporate shareholders (equity holders). A claim for contribution and indemnity in respect of a claim for a monetary loss resulting from the ownership, purchase or sale of shares falls squarely within the examples of equity claims expressly provided for in the definition of equity claims under s. 2 of the BIA. In *Sino Forest*, the Court's expanded view was in its recognition that the auditors' claim grounded in a cause of action for breach of contract did not change its essential character as a claim for contribution and indemnity in respect of shareholder (equity) claims.

[57] In each case cited by the Proposal Trustee where a claim has been found to be an equity claim, it was in some way related to a direct or indirect equity interest within the meaning of the BIA.

a. *Sino-Forest* concerned a claim for contribution and indemnity relating to a shareholder class action.

b. *Bul River Mineral Corporation (Re)*, 2014 BCSC 1732, 16 C.B.R. (6th) 173 concerned a shareholder's claim against the debtor that had been reduced to a court judgment before the bankruptcy filing.

c. *Return on Innovation v. Gandi Innovations*, 2011 ONSC 5018, 83 C.B.R. (5th) 123 involved a claim relating to the recovery of a $50 million dollar equity investment through an arbitration.

d. *US Steel Canada Inc. (Re)*, 2016 ONSC 569, 34 C.B.R. (6th) 226 concerned a claim relating to the recovery of loans advanced by the parent company/sole shareholder of the debtor.

e. *Tudor Sales Ltd. (Re)*, 2017 BCSC 119, 44 C.B.R. (6th) 45 concerned a claim relating to advances made by a shareholder of the debtor and its sole officer and director.

f. *YG Limited Partnership and YSL Residences (Re)*, 2021 ONSC 4178, 93 C.B.R. (6th) 109 (Dunphy J.'s judgment declining to approve the proposal, referred to earlier) concerned claims brought by parties related to Cresford that had an equity interest in the YSL Project.

[58] The suggested approach of the Proposal Trustee relies upon *Re Central Capital Corp.* (1996), 27 O.R. (3d) 494 (C.A.), at para. 67 and *Re Canada Deposit Insurance Corp.* [1992] 3 S.C.R. 558). These cases were decided before there was a statutory definition of "equity claim". They seek to characterize a claim as debt or equity by looking at "the surrounding circumstances to determine whether the true nature of the relationship is that of a shareholder who has equity or whether it is that of a creditor owed a debt or liability by the company". In *Sino-Forest* (at para. 53) the court stated that the statutory definition of equity claim "is sufficiently clear to alter the pre-existing common law". Thus, the earlier approach adopted in these cases is not instructive.

[59] Even if profit sharing has equity features, there is no evidence or suggestion that the Profit Sharing Agreement granted, or in any way relates to the granting of, shares or rights to acquire shares in YSL or any of the Cresford Group of companies to Ms. Athanasoulis. There is no evidence or finding that Ms. Athanasoulis was a shareholder or held any right to become a shareholder. Nor is her claim for contribution and indemnity in respect of ownership or equity rights.

[60] The only connection to equity or ownership is her acknowledgement that the Profit Share Claim is to be calculated as a percentage of the profits that would otherwise be payable to the

Cresford Group Class B unitholders[2] comprised of Mr. Casey and his family members (the ultimate owner/developer of the YSL Project and the Cresford Group). Ms. Athanasoulis' testimony at the Arbitration was that the profit under the Profit Sharing Agreement "would be calculated after paying the [specific project] costs and after the equity was repaid to the LP Investors". She testified that profits were to be calculated as revenues less expenses, consistent with the YSL Project pro formas, which included among the other expenses or project costs the repayment of funds advanced by the LPs.

[61] A claim by terminated employees for damages in respect of incentive-based compensation, including where such compensation is calculated with reference to sales or profitability, can be, and has been, successfully pursued as a claim for damages against a bankrupt company. See *Noble v. Principal Consultants Ltd. (Trustee of)*, 2000 ABCA 133, 17 C.B.R. (4th) 274, at paras. 41–42.

[62] The fact that the parties chose to tie the quantification of the amounts payable under the Profit Sharing Agreement to the YSL's (and the Cresford Group') performance (profits, after deducting, or net of, amounts payable to the LPs) does not transform a contractual obligation or debt to Ms. Athanasoulis into an equity claim within the meaning of the BIA, even if the practical effect of this would have been that payments under the Profit Sharing Agreement in the normal course would be made after payments to the LPs.

[63] The present situation did not arise in the normal course and was not specifically contemplated when the Profit Sharing Agreement was made. As the Arbitral Award found (at para. 147), "it is not essential to the enforceability of the agreement that every option regarding the calculation of profits be affirmed or negated" at the time it is made.

[64] The definition of equity claim under the BIA is clearly and unequivocally a claim in respect of shares or rights to acquire shares in a company. There is no suggestion that the Profit Share Claim is in respect of that type of interest. At best, it is a claim to be calculated based on the residual profits remaining in YSL that would otherwise be available to be distributed or paid to the Cresford Group, the ultimate owners or equity holders. The calculation of this claim based on profits is separate and distinct from a claim in respect of shares or the right to acquire shares.

[65] The concept of an equity claim "in substance" was introduced into the Notice of Disallowance by the Proposal Trustee. There is no concept of an equity claim "in substance" under the BIA, even giving the definition of equity claim an expansive meaning.

[66] The Proposal Trustee made an extricable error in law by expanding the definition of "equity claim" under the BIA to a claim that is not in respect of an equity interest (shares or the right to

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[2] These Cresford Group members are referred to by the parties sometimes as shareholders and sometimes as unitholders, but always with the understanding that they have the status of shareholders or equity holders for purposes of this decision.

acquire shares or an ownership interest in YSL) within the meaning of s. 2 of the BIA. This determination is reviewable on the standard of correctness.

[67] Having regard to the definitions of "equity claim" and "equity interest" under the BIA, I find that the Profit Share Claim is not an equity claim within the meaning of the BIA.

ii. Contingent vs. Unliquidated Damages Claim and Remoteness

[68] There are two aspects to the Proposal Trustee's determination that the Profit Share Claim is a contingent claim that is too speculative or remote. The first requires consideration of the distinction between a contingent claim and an unliquidated claim. The second requires consideration of the remoteness of damages more generally.

[69] The cases relied upon by the Proposal Trustee dealing with contingent claims that were found to be too remote and speculative to be provable claims in a bankruptcy are all claims that were contingent upon a future uncertain event that had not yet occurred and was not inevitable. As the Supreme Court held in *Newfoundland and Labrador v. AbitibiBowater Inc*., 2012 SCC 67, [2012] 3 S.C.R. 443, at para. 36, the determination of whether such contingent claims are provable claims depends on "whether the event that has not yet occurred is too remote or speculative". See also *Orphan Well Association v. Grant Thornton Ltd.*, 2019 SCC 5, [2019] 1 S.C.R. 150, at para. 138.

[70] Here, the hypothetical contingency that the Proposal Trustee relies upon was whether any profits would be earned by YSL or any other entities in the Cresford Group: unless and until there were profits (calculated after repayment of the amounts advanced by the LPs), there would be nothing to share under the Profit Sharing Agreement. That hypothetical contingency assumes the continuation of the Profit Sharing Agreement.

[71] However, the Arbitrator found that Ms. Athanasoulis' employment contract was repudiated in December 2019 and found that the Profit Sharing Agreement was part of that integral contract of employment (and her employment compensation). The Arbitrator also found that her entitlement to compensation under the Profit Share Agreement was not dependent upon her continued employment (in other words, that compensation could not be avoided by her termination). While no express finding was made that the Profit Share Agreement was breached, it follows from these findings that the Profit Sharing Agreement, an integral part of her employment contact, was also repudiated when she was constructively dismissed.

[72] Ms. Athanasoulis accepted the repudiation by YSL in early January 2020 and she sued YSL (and others) for breach of contract and damages, including damages in respect of the Profit Sharing Agreement, in January 2020.[3] In her January 21, 2020 Statement of Claim she claimed

[3] Little was said in the course of submissions about the parallel civil proceedings between Ms. Athanasoulis and the Cresford Group and between the LPs and the Cresford Group and Ms. Athanasoulis, although it was generally agreed

damages for, among other things, breach of the Profit Sharing Agreement equal to 20% of what she estimated the anticipated profits would be on all projects, the most significant of which was YSL.

[73] Until there was a breach, the Profit Sharing Agreement would remain in place and any claim for payment under that agreement might reasonably be considered to be contingent upon profits actually being earned (to be calculated based on revenues less expenses, where expenses would include any amounts payable to the LPs). It might have been open to Ms. Athanasoulis not to accept the repudiation of the Profit Sharing Agreement and let it continue even though she was no longer employed by YSL and wait to be paid in the normal course, but she clearly did the opposite, as evidenced by her civil claim for damages for breach of that agreement commenced in January 2020.[4]

[74] As a matter of law, the accepted repudiation of the Profit Sharing Agreement converted a future right to receive actual profits if and when earned into a current right to receive damages for breach of contract. Once converted to a damages claim, the "normal course" that Ms. Athanasoulis would be paid once the profits had been earned, usually at the end of a project, no longer applied. Rather, the Profit Share Claim became an unliquidated claim for damages for breach of contract that would presumptively be assessed at the time of repudiation. This is explained in more detail later in this endorsement.

[75] The Proposal Trustee made an extricable error in law by characterizing the Profit Share Claim, which is a claim for unliquidated damages for breach of contract, as a contingent claim dependent upon actual profits having been or being earned.

[76] The erroneous characterization of the Profit Share Claim as a contingent claim led the Proposal Trustee to the further erroneous determination that it, as contingent claims often are, was too remote and speculative to be a "provable" claim under the BIA.[5]

[77] I turn to the second aspect of the remoteness of the Profit Share Claim. Even if not a contingent claim dependent upon an event that has not occurred, unliquidated claims are still subject to quantification and related considerations of remoteness or speculation.

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that those proceedings would be subject to arguments of *res judicata* and estoppel if determinations are made on this appeal in respect of any overlapping issues involving the same parties.

[4] Even if the Profit Sharing Agreement continued, the Profit Share Claim might still have been a provable claim. The court in *Abitibi* held (at para. 34) that "the broad definition of "claim" in the BIA includes *contingent and future* claims that would be unenforceable at common law or in the civil law."

[5] If a claim is contingent, the claimant must demonstrate sufficient certainty that the contingency will occur during the relevant period for the damages calculation. See *Abitibi* at para. 36 and 84 and *Confederation Treasury Services Ltd., Re* (1997), 96 O.A.C. 75 (C.A.), at para. 4.

[78] The court in *Abitibi* specifically found at para. 34 (in the context of a CCAA proceeding) that a court (in that case, the CCAA court) assessing unliquidated claims in statutory insolvency proceedings "has the same power to assess their amounts as would a court hearing a case in a common law or civil law context." The Profit Share Claim should be viewed under the same lens in terms of its provability.

[79] The Court of Appeal explained in *Schnier v. Canada (Attorney General)*, 2016 ONCA 5, 128 O.R. (3d) 537, at para. 49, that "a creditor's inability to enforce a claim bears directly on the creditor's ability to prove its claim under the BIA. In order to be a provable claim within the meaning of BIA s. 121, a claim must be one recoverable by legal process". Ms. Athanasoulis says her Profit Share Claim is recoverable by legal process, and that was the very course she was following by the lawsuit that she commenced in January 2020.

[80] In *Schnier*, the court found the opposite because the claim in that case was dependent upon the outcome of ongoing tax proceedings. The Proposal Trustee seeks to analogize the Profit Share Claim (said to be dependent upon the outcome of litigation that Ms. Athanasoulis had commenced following her wrongful dismissal from YSL, and thus contingent in that sense) to the situation in *Schnier*. The analogy is not apt, for various reasons including that:

a. *Schnier* was about whether the special provisions of the BIA regarding income-tax driven bankruptcies applied to unpaid tax assessments that were being appealed. The trustee had found that the tax claim in question was not provable. That finding was not challenged (at para. 14). The court conducted a detailed review of the statutory scheme and concluded that those rules were not meant to be triggered by contingent tax claims that the trustee has determined to be unproven (see paras. 24–50 and 73).

b. The mere fact that a disputed claim is in litigation but has not yet resulted in a judgment cannot be sufficient to render a claim unprovable under the BIA. If that were the case, it would mean that anyone who claims to have been wronged by a debtor would be disqualified from making a claim in a bankruptcy proceeding if they had not been able to obtain a pre-BIA judgment.

c. Through the Arbitration, it has already been established in this case that there was an oral Profit Sharing Agreement that was part of Ms. Athanasoulis' employment agreement, that she was wrongfully (constructively) dismissed in December 2019 and that her Profit Sharing Agreement did not depend upon her continuing to be employed. Her claim for damages arising out of the breach of that agreement is a claim that is recoverable by legal process even if that legal process has not yet run its course.

[81] The Proposal Trustee considered the potential for damages associated with the Profit Share Claim insofar as that might inform the assessment of whether it is too remote or speculative to be a provable claim. Even if it is not a contingent claim, the Proposal Trustee determined that the Profit Share Claim is too remote and speculative to qualify as a provable claim because it seeks:

a. a share of the profits in a failed project that never did, and never will, generate any profits; and

b. profits to be calculated on the basis of an agreed formula that assumes that the amounts owing to the LPs will be treated as expenses and netted out of the calculated profits even though they have not been paid and are not expected to be paid in full under any scenario.

[82] The Proposal Trustee points to the earlier findings of Hainey J. (in an insolvency proceeding involving a different Cresford entity) and Dunphy J. in this proceeding that Ms. Athanasoulis' Profit Share Claim was too speculative or remote to be valued for voting purposes. However, those earlier determinations were made at a time when there was uncertainty about the existence of the Profit Sharing Agreement and about whether Ms. Athanasoulis had been wrongfully terminated from her employment. Those aspects of the claim are no longer subject to speculation. I do not consider those earlier assessments to be determinative of the question of whether the Profit Share Claim is too remote or speculative to be provable. That must be independently assessed in the context of the Disallowance.

[83] The Proposal Trustee's rationales for the Profit Share Claim being too remote or speculative (above) are, in part, a function of its original error in having failed to recognize it to be an unliquidated damages claim for breach of contract. This resulted in a compounding further extricable error of law because it led the Proposal Trustee not to consider the well-established legal principle that damages for breach of contract are presumptively to be calculated at the date of breach. See *Kinbauri Gold Corp. v. Iamgold International African Mining Gold Corp.* (2004), 192 O.A.C. 24 (C.A.), at para. 125; see also *Kipfinch Developments Ltd. v. Westwood Mall (Mississauga) Limited*, 2010 ONCA 45, 260 O.A.C. 110, at para. 15; *Baud Corp., N.V. v. Brook* (1978), [1979] 1 S.C.R. 633, at p. 648.

[84] The value of the promised performance is measured by evaluating what would have happened if the contract had been performed. The correct approach is illustrated in *Performance Industries Ltd. v. Sylvan Lake Golf & Tennis Club Ltd.*, 2002 SCC 19, [2002] 1 S.C.R. 678. In that case, one party to an option agreement breached the contract and, as a result, the other party lost the opportunity to develop the land. The Supreme Court of Canada upheld the trial judge's award of the profits that the wronged party would have made. In *Sylvan* no one actually earned profits. But that did not matter.

[85] The Proposal Trustee points out in response to these submissions on the appeal that the presumptive date for assessing damages (as of the date of the breach) is not an absolute. The Court of Appeal has departed from this presumptive date in appropriate circumstances, such as in *Maple Leaf Foods Inc. v. Ryanview Farms*, 2022 ONCA 532, at paras. 35 and 41. In that case, it was found that the assessment of damages at the date of breach would not fairly reflect a party's loss in light of intervening events rendering the loss suffered to be more uncertain, such that it would not be just to burden the breaching party with more than its fair share of the liability.

[86] On this appeal, the Proposal Trustee suggested that it considered that the COVID-19 pandemic, record inflation, rapidly increasing interest rates, the state of the real estate market and the fact that YSL became insolvent and entered into these proposal proceedings all would have

adversely affected the profitability of YSL even if Ms. Athanasoulis had never been constructively dismissed. Thus, the consideration of what would have happened if the Profit Share Agreement had not been repudiated still would lead to the conclusion that the prospect of any damages is too remote and speculative for there to be any provable loss.

[87] Ms. Athanasoulis points out that these considerations were not all set out in the stated grounds for the Disallowance of her Profit Share Claim and would, at most, be factors that might be considered in the eventual valuation of her Profit Share Claim, but not grounds for the Disallowance without any attempt to value it.

[88] As previously outlined, absent a breach and in the normal course Ms. Athanasoulis would have been paid out of YSL's earned profits, and the timing of the actual payments to the LPs and to Ms. Athanasoulis would have followed the completion of the YSL Project. However, when YSL repudiated the Profit Share Agreement and the repudiation was accepted as of January 2020, Ms. Athanasoulis' future right to receive a 20% share of earned profits was converted into a current right to receive damages for breach of contract. If the appropriate approach to the assessment of damages had been adopted, speculation and concerns about the remoteness of those future events (the actual profits that may or may not be earned, and the order in which they might have been distributed in the normal course) might not be relevant at all to the determination of the Profit Share Claim under the BIA, but even if relevant at the valuation stage, those concerns would not be determinative at this threshold "provability" stage in the face of the presumptive valuation date.

[89] There are two branches to remoteness in assessing damages, that have to do with the type of loss at issue. In *The Rosseau Group Inc. v. 2528061 Ontario Inc.*, 2023 ONCA 814 at paras. 68–70, the Court of Appeal reminds us that damages will not be considered to be too remote and may be recovered if:

a. In the "usual course of things", they arise fairly, reasonably, and naturally as a result of the breach of contract; or

b. They were within the reasonable contemplation of the parties at the time of contract.

Damages that fall outside of either branch are not recoverable because they are too remote.

[90] Importantly, the Court of Appeal explains in *The Rosseau Group* (at para. 70) that "the remoteness test deals with the 'type' of loss that is recoverable, while the measure is about how it is quantified." The type of loss at issue here is in respect of the lost opportunity to contribute to and eventually share in the profits that the parties anticipated would eventually be earned by YSL when the YSL Project was completed. The remoteness concerns identified by the Proposal Trustee are in respect of the measure of the damages, not the type of loss.

[91] There is a well-established legal principle that a party should not be denied damages just because those damages are difficult to calculate or measure. See *General Mills Canada Ltd. v. Maple Leaf Mills Ltd.*, 52 C.P.R. (2d) 218 (Ont. H. Ct.), at para. 4; *Gould Outdoor Advertising Co. v. Clark*, [1994] O.J. No. 3094 (Gen. Div.), at para. 26. In such cases, damages are assessed with a broad axe and a sound imagination. See *Colonial Fastener Co. Ltd. v. Lightning Fastener Co. Ltd.*, [1937] S.C.R. 36, at p. 44; *Apotex Inc. v. Eli Lilly and Company*, 2018 FCA 217, 161 C.P.R.

(4th) 411, at para. 142; *Janssen Inc. v. Teva Canada Limited*, 2016 FC 593, 141 C.P.R. (4th) 1, at para. 69. This is an issue for another day in these proceedings.

[92] The Proposal Trustee's consideration of subsequent events in its determination that the Profit Share Claim is not a provable claim under the BIA was an extricable error of law. While those subsequent events may be relevant to the measure or calculation of the ultimate loss, to say that they affect the type of loss and render it so remote as to be unprovable results in a misapplication of the law of remoteness.

[93] The bar for establishing a provable claim is low and only requires that a claimant proves that there is an "air of reality" to their claim. See *Oil Lift Technology Inc. v. Deloitte & Touche Inc.*, 2012 ABQB 357, 98 C.B.R. (5th) 77, at para. 18. There is an air of reality to the Profit Share Claim, particularly since the Arbitrator has determined that: the Profit Sharing Agreement existed, it was a key element of Ms. Athanasoulis' employment contract, Ms. Athanasoulis was constructively terminated from her employment in December 2019, but the Profit Sharing Agreement was not dependent upon her continuing to be employed. The fact that a claim involves some complexity in quantification is not a bar to it being a provable claim.

[94] Considering the Profit Share Claim in its proper light (which the Proposal Trustee did not do as a result of its previously identified errors), I find it to be a provable claim.

B) The Valuation Errors

[95] Ms. Athanasoulis alleges that it was an error for the Proposal Trustee to value her Profit Share Claim at zero based on the determination that there was no profit to share, as at the date of the breach (December 2019), the date of these insolvency proceedings (April 2021) or two years after the breach when her claimed employment termination notice period ran out (December 2021), because doing so was predicated on the absence of any actual, earned profits on any of these dates.

[96] It is alleged that the Proposal Trustee erred in valuing the Profit Share Claim at zero:

a. Based on the erroneous assumption that Ms. Athanasoulis is only entitled to 20% of the actual profits earned by YSL or that YSL is capable of earning in light of its insolvency and the Proposal, whereas damages for breach of contract must put the injured party in the position she would be in if the other party had met its contractual obligations, calculated at the time of the breach or repudiation of the contract;

b. Without even attempting to calculate either YSL's revenues or expenses to determine its profits earned on the relevant date (of repudiation);

c. Without considering contemporaneous evidence (on the repudiation date) about the prospect of a sale of the YSL Project or YSL's contemporaneous pro forma projections for continued development that indicate a reasonable expectation of profits.

[97] The Arbitrator's finding that Ms. Athanasoulis' employment contract, of which the Profit Sharing Agreement was found to have been an integral part, was breached in December 2019 crystalized her claim for damages for breach of the Profit Sharing Agreement. No assessment was

undertaken of what her loss was as of that date, to put her in the position she would have been in if the Profit Sharing Agreement had not been breached in December 2019. The Proposal Trustee did not undertake this exercise because her losses were assumed to be zero given that no profits have been or will be earned by YSL. This approach built upon the previously described errors in the mischaracterization of the Profit Share Claim. Much of the same analysis applies to here to the Valuation Errors, as was applied to the Provable Claim Errors discussed in the previous section of this endorsement.

[98] The Proposal Trustee's answer to this, when considered from a claim valuation (as opposed to provability) perspective, is to treat the Profit Share Claim as part of the Wrongful Dismissal Claim, such that Ms. Athanasoulis would only be entitled to reasonably foreseeable amounts payable under the Profit Sharing Agreement during her claimed termination notice period (specified in her statement of claim issued in January 2020 to be two years). This approach was adopted based on the case of *Matthews v. Ocean Nutrition Canada Ltd.*, 2020 SCC 26, [2020] 3 S.C.R. 64, at para. 49 involving a terminated employee whose profit sharing agreement was found to have been limited to actual profits earned during the notice period. Since the YSL Project was not completed and no profits were earned or paid out by it during that notice period, nor would the parties have expected them to be given the usual five to seven year completion period for a project such as the YSL Project, the Proposal Trustee maintains that there could be no damages or losses suffered as a result of the repudiation of the Profit Share Agreement.

[99] However, there is an important distinguishing feature of this case compared to *Matthews*. In *Matthews*, the profit sharing was expressly tied to his continued employment (see para. 63). In *Matthews*, there was a long-term incentive plan that required the claimant to be employed full time at time of triggering event (sale), but he had been constructively terminated 13 months before (para. 18).

[100] The Proposal Trustee's position is that the Arbitrator's finding that entitlements under the Profit Sharing Agreement are not dependent upon Ms. Athanasoulis' continued employment with YSL (or equivalent notice period) should not give her an indefinite claim to 20% of any and all profits earned, beyond the notice period. However, this position is not tied to any finding of fact or legal principle.

[101] Conversely, even if Ms. Athanasoulis had been given two-years working notice and her employment had then terminated, it is not a given that her entitlements under the Profit Sharing Agreement would have automatically ended. The preservation of entitlement under the Profit Sharing Agreement is consistent with the Arbitrator's finding that the Profit Sharing Agreement was intended to recognize her past and continuing contributions and was not just an incentive for future contributions. The Arbitrator expressly found that YSL could not eliminate Ms. Athanasoulis' claim by terminating her and could not reduce her share to zero after her prior years of contributions in the form of advance sales, etc. simply by terminating her employment on notice (at para. 160). It follows from these findings of the Arbitrator that, unlike in *Matthews*, the termination notice period is not determinative of the Profit Share Claim.

[102] Further, the fact that these voluntary insolvency proceedings occurred is not evidence that they were inevitable. Dunphy J. specifically found that the effort to sell or refinance the YSL Project that culminated in the earlier proposal was "indelibly tainted" by Mr. Casey's self-interest

(see *YG Limited Partnership and YSL Residences (Re)*, 2021 ONSC 4178, 93 C.B.R. (6th) 109, at para. 76).

[103] The Proposal Trustee's determination that, with no profits having been earned during the two-year notice period or thereafter, the damages for the repudiation of the Profit Share Claim are zero, was an extricable error of law. In order to justify this conclusion, the Trustee departed from the law of damages for breach of contract.

[104] The Trustee also relies upon equity, by arguing that it is not "just and reasonable" to calculate profits on the repudiation date because "no profit had been earned" and the LPs had not been repaid. This is not grounded in any authority, but if relevant at all it would arise in the context of the calculation of the loss and valuation of the claim, not at this threshold stage before any attempt has been made to value the Profit Share Claim. That too was an extricable error of law.

[105] Even if the Valuation Errors involve a misapplication of the law to the facts, which might be viewed as mixed errors rather than extricable errors of law, those errors were palpable and overriding in this case.

[106] In this vein, in addition to the extricable legal errors, Ms. Athanasoulis argues that there is evidence to contradict the Proposal Trustee's underlying factual assumptions. The failure to consider that evidence is reviewable on a standard of palpable and overriding error (or reasonableness). However, given the findings to this point, there is no need to go into an in-depth analysis of what are errors of fact and mixed fact and law.

[107] The primary point that is made by Ms. Athanasoulis at this stage is that the Proposal Trustee has not done any in-depth analysis to attempt to assess the damages as at the date of repudiation. It is sufficient for purposes of this appeal to have identified that there will be points of contention to be considered when the Profit Share Claim is valued, for example:

a. According to Ms. Athanasoulis, when she was terminated the YSL Project had progressed significantly. The YSL Project was purchased for $157 million but was appraised in July 2019 for $375 million. YSL had invested approximately $241 million in the project. YSL's October 2019 pro forma, which had been vetted by experienced third party professionals, forecast a profit of close to $200 million. Even the Proposal Trustee's third report implies YSL was profitable. Further, Ms. Athanasoulis points to contemporaneous evidence about the prospect of a sale of the YSL Project. According to her testimony, there was a buyer for the YSL Project that would have yielded profits, who Casey inexplicably rejected around the time of her wrongful dismissal. She claims that, at that time, YSL was fine financially and that it was other Cresford projects that were in trouble.

b. The Proposal Trustee points to a letter that Ms. Athanasoulis wrote in December 2019 about ongoing financial issues. She has since admitted that there were statements made in that letter that were untrue and she has apologized for sending it. However, the Proposal Trustee says it is evidence from Ms. Athanasoulis herself about the dire financial situation that YSL and the Cresford Group were in at that time.

c. The Proposal Trustee urges the court to look at other contemporaneous evidence that had been in the Arbitration record to counter the evidence Ms. Athanasoulis put forward and the anticipated profitability of the YSL Project at the time of the Profit Sharing Agreement. The Proposal Trustee points to high-level financial information that it says demonstrates that YSL was underwater in December 2019 (and that is consistent with its eventual insolvency). Ms. Athanasoulis objected to the Proposal Trustee's last-minute reliance upon this evidence, that was not a stated basis for the Disallowance of her Profit Share Claim and that she claims is selective and unreliable. For example, certain of the reports referenced had been previously ruled to be unreliable by Dunphy J. and another expresses opinions about the value of the YSL Project as at May 2021 which is after the December 2019 repudiation date.

[108] At this stage in these proceedings where the damages have been bifurcated in accordance with the court's earlier Claims Procedure Endorsement, it is sufficient for Ms. Athanasoulis to have demonstrated that damages could be calculated (based on either actual profits earned as of the date of contract repudiation or "but-for", future oriented profits calculated, possibly with the assistance of expert evidence, as at that date), since it was not intended that there be a valuation of the Profit Share Claim at this stage. The very existence of this evidentiary controversy is itself reason to require a more fulsome damages assessment, as the Claims Procedure Endorsement provides for.

[109] Sufficient grounds have been established to satisfy me that the damages valuation phase should proceed.

C) Subordination Error

[110] Ms. Athanasoulis' testimony at the Arbitration that the profit under the Profit Sharing Agreement "would be calculated after paying the [specific project] costs and after the equity was repaid to the LP Investors" led the Proposal Trustee to conclude that the Profit Share Claim was an equity claim that was subordinated to the equity claims of the LPs. For the reasons previously indicated, the Profit Share Claim does not come within the BIA definition of "equity claim". Not all entitlements calculated on the basis of profits are equity claims. The formula used to calculate the amount of an entitlement is also not determinative of the priority of a claim in a bankruptcy. Here, the calculation of the entitlement under the Profit Sharing Agreement was to be based on a percentage of funds distributable to the owners (equity holders) whose claims were subordinated to the LPs. That does not mean that the Profit Share Claim was subordinated.

[111] The LPs assert that Ms. Athanasoulis (and others) told them that they would be paid ahead of the Cresford Group , who were themselves Class B unitholders. However, Ms. Athanasoulis was not a shareholder. Nor did she enter into any agreement directly with the LPs to subordinate her claims or interests to theirs.

[112] The Proposal Trustee made an extricable error of law when it found the Profit Share Claim to be subordinated to the equity claims of the LPs and that Ms. Athanasoulis is not entitled to be paid anything unless and until the LPs are paid in full, in the absence of any agreement between Ms. Athanasoulis and the LPs to subordinate her claims to theirs.

[113] This error originated from the same incorrect determination that led to earlier errors, namely that all claims calculated based on profits are equity claims. It was further compounded by the incorrect conclusion that by agreeing with YSL and the Cresford Group that the profits to which the 20% profit sharing would be applied would be calculated net of amounts to be paid to the LPs, Ms. Athanasoulis had agreed to subordinate her entitlements under the Profit Sharing Agreement to the claims of the LPs claims for insolvency and BIA purposes.

[114] It is common ground that each LP holds an "equity claim" within the meaning of the BIA. The BIA provides that every creditor who does not hold an "equity claim" is entitled to be paid before any creditor that has an equity claim. These statutory priorities were ignored by the Proposal Trustee because of the error in mis-characterizing the Profit Share Claim (entitlements under the Profit Sharing Agreement) as an equity claim.

D) Other Identified Errors

[115] Other errors were identified by Ms. Athanasoulis. However, the appeal can be decided based on the identified extricable errors of law (above).

The Unique Perspective of the LPs on the Validity/Enforceability of the Profit Sharing Agreement

[116] The LPs argue that there are specific provisions in two contracts that they entered into that render the Profit Sharing Agreement unenforceable, namely that the Profit Sharing Agreement:

a. breaches s. 3.6(b) of the Amended and Restated Limited Partnership Agreement dated August 4, 2017 (the "LPA") that prohibits non-arm's length transactions with a "Related Party" (meaning the Affiliates of the General Partner in the sense of controlling or controlled by or under common control with, YSL and their officers and directors, employees and shareholders) other than on market terms; and

b. breaches s. 3.2 of the Sales Management Agreement dated February 16, 2016 (the "Management Agreement") that prohibits any compensation being paid to the corporation or its Affiliates (defined under the LPA to be the Affiliates of the General Partner in the sense of controlling or controlled by, or under common control with, YSL) that is not specifically provided for in that agreement (and there is no reference to the Profit Sharing Agreement).

[117] These are the matters that the LPs were granted standing to address in the Claims Procedure Endorsement. They provided their submissions to the Proposal Trustee on these (and other) issues. These grounds were not adopted or relied upon by the Proposal Trustee as a reason for its Disallowance of the Profit Share Claim. There is no reviewable error by the Proposal Trustee in relation to the LPs' submissions.

[118] In terms of the merits of the LPs arguments if they are to be addressed *de novo*, there is no evidentiary foundation for the suggestion that Ms. Athanasoulis is an Affiliate of YSL that would render the Profit Sharing Agreement to be offside of s. 3.2 of the Management Agreement. Ms. Athanasoulis maintains that she was neither a shareholder nor an affiliate of the Cresford Group and was never represented to be such in any written or oral presentation made to the LPs, nor is it

apparent on what legal basis a declaration of unenforceability would be the appropriate remedy for such a breach, in any event. The alleged breaches of Management Agreement appear to have been an after-thought (not mentioned in the LPs' factum on this appeal). There is no basis upon which to find that the Profit Sharing Agreement was a breach of the Management Agreement.

[119] It has also not been established that the Profit Sharing Agreement constitutes a prohibited Related Party agreement under s. 3.6(b) of the LPA. The Profit Sharing Agreement was entered into before the LPA, although the percentage of shared profits increased after the LPA was signed). The LPs claim not to have been told about either the original or amended Profit Sharing Agreement. The Profit Sharing Agreement was found by the Arbitrator to be binding and enforceable as between the parties to it, YSL and Ms. Athanasoulis.

[120] The LPs have presented no evidence to establish that the Profit Sharing Agreement was not on market terms. The Arbitrator found that there was "nothing disproportionate, in the realm of executive compensation," about the Profit Sharing Agreement, in light of Ms. Athanasoulis' value and contributions to the YSL Project (and the Cresford Group's other projects). The evidence before the Arbitrator was that a third party marketing company would have charged 1.5% of sales and expected to have been paid earlier. The LPs were not party to the Profit Sharing Agreement and complain that they were not party to the Arbitration and should not be bound by findings made by the Arbitrator. If the LPs had wanted the court to revisit that determination for purposes of this appeal that would have required some further direct evidence.

[121] There is no basis upon which the court could or should conclude based on the record on this appeal that the Profit Sharing Agreement is unenforceable as a result of the alleged breaches of the LPA and the Sales Management Agreement. These arguments raised by the LPs do not affect the court's determinations earlier in this endorsement that the Profit Sharing Claim is a provable claim and should be valued.

Additional Issues Raised by the LPs

[122] The LPs claim that the Profit Sharing Agreement was a "secret" undisclosed agreement. They assert that she made misrepresentations by omission (by not disclosing the existence and terms of the Profit Sharing Agreement). They claim that statements made by Ms. Athanasoulis regarding the priority of payments to the LPs over any payments out to Cresford Group members were misleading if they were not intended to include payments to Ms. Athanasoulis, who they (rightly or wrongly) understood to be a member of the Cresford Group. They say they were induced to advance funds as a result of these representations. They assert that even if she owed no duty to them directly, she knowingly assisted in the alleged misrepresentations made to them by others.

[123] The LPs rely on cases that extend fiduciary disclosure duties and duties not to self-deal to general partners and their directors and officers such as *Naramalta Development Corp. v. Therapy General Partner Ltd.* 2012 BCSC 191, at paras. 63–64 and 71–72; *OSC v. Go-to Developments Holdings Inc.* (October 31, 2023), Toronto, CV-21-00673521(S.C.), *per* Steele J.; *Advanced Realty Funding Corp. v. Bannink* (1979), 27 O.R. (2d) 193 (C.A.); and *Extreme Venture Partners Fund 1 LP v. Varma*, 2021 ONCA 853, 24 B.L.R. (6th) 38, at paras. 74 and 86–89, leave to appeal refused.

[124] Ms. Athanasoulis denies that the existence of the Profit Sharing Agreement renders her statements about the Cresford Group to be untrue or misleading. Further, she denies any duty to make disclosure and argues that this situation (that she and the LPs would be competing for the same pool of funds) was not reasonably foreseeable. In any event, these alleged misrepresentations are not properly raised in the context of the Proposal Trustee's determination of the validity and quantum of the Profit Share Claim.

[125] The 250 LPs have commenced a separate lawsuit against Ms. Athanasoulis, and others, asserting claims against them personally in respect of the alleged misrepresentations and breaches of fiduciary and other duties arising out of the failure to disclose her Profit Sharing Agreement to them. All of the LPs have raised these issues with the Proposal Trustee as further grounds for disallowing her Profit Share Claim, but their allegations were not among the grounds relied upon in the Disallowance.

[126] While the 250 LPs confirmed that there would be a *res judicata* or estoppel argument against re-litigating these claims in another context if the court decides these issues in this appeal, there remains the more fundamental concern that these issues fall outside of the scope of the standing that was granted to the LPs in the context of the Profit Share Claim, which was to raise issues that they were uniquely situated to address relating to the determination of that claim. Those issues include matters relating to the validity and enforceability of the Profit Share Agreement having regard to the provisions and restrictions under the agreements that the LPs were party to, such as the LPA and the Management Agreement. Those grounds have been addressed in the preceding section of this endorsement.

[127] The other claims of the LPs, which include an estoppel argument arising out of the alleged misrepresentations and breaches of duties by Ms. Athanasoulis, or her alleged knowing assistance of breaches by others, are not properly adjudicated in the context of the determination and valuation of the Profit Share Claim. Further, Ms. Athanasoulis points out that the LPs have not put forward evidence of their reliance on the representations to enable any ruling to be made in their favour.

[128] The mere allegation of an "omission" to make disclosure is not sufficient to determine their claims in the circumstances of this case. Not only is there a dispute about Ms. Athanasoulis' status as a member of the "Cresford Group", but the LPAs expressly preclude reliance upon extra-contractual representations. The facts surrounding these allegations against Ms. Athanasoulis are not settled, which could explain why this was not one of the reasons relied upon by the Proposal Trustee in the disallowance of the Profit Share Claim. This case is distinguishable from *OSC v. Go-To Developments Holdings Inc.*, at paras. 10-16; 25-26 that the LPs seek to rely upon, involving alleged misrepresentations made by a director and shareholder.

[129] This is not the forum for determining those other claims by the LPs. The determination of those claims involves contentious factual disputes and credibility assessments. The issues raised by the LPs cannot be properly adjudicated in a summary fashion on a paper record in the context of this appeal. Ultimately, these are matters that are more properly addressed between Ms. Athanasoulis and the LPs outside of the context of these insolvency proceedings. It would not be reasonable or appropriate for the court to attempt to determine the LPs' claims for breach of fiduciary duty and misrepresentation, etc. on this appeal.

[130] These claims by the LPs (for alleged misrepresentations, breaches of fiduciary and other duties, estoppel and knowing assistance) are extraneous to the Trustee's Disallowance and to any future valuation of the Profit Share Claim. It may be that the valuation of the Profit Share Claim for purposes of the BIA process could have some bearing upon those other claims, but that is an issue for another day and another court.[6]

[131] However, findings have been made regarding the enforceability and validity of the Profit Sharing Agreement and the subordination issue for purposes of the determination of priority of claims in these BIA proceedings and will be binding upon the LPs in any future proceedings.

Valuation and Damages

[132] At paragraph 63 of the Claims Procedure Endorsement, the court clarified that:

> To be clear, it is not expected that there will be any material or submissions at this time regarding the Future Oriented Damages (whether calculated at the repudiation date or the Proposal date). If Ms. Athanasoulis is successful on appeal of any disallowance of the Profit Share Claim, the parties shall make an appointment for a case conference before me (if my schedule permits within the time frame requested) to seek directions about the process for the determination of the more complex valuation question that will likely require expert input.

[133] Since Ms. Athanasoulis has succeeded on her appeal of the Disallowance, the Profit Share Claim needs to be valued. The Profit Share Claim is a claim for unliquidated damages for the breach of the Profit Sharing Agreement in December 2019 that was accepted in January 2020 (by correspondence and eventually the issuance of a statement of claim seeking to recover damages for this breach, among other damages). The April 30, 2021 bankruptcy date may also be relevant to this determination. The relevance and impact of intervening events remains an open question. Expert inputs may be appropriate on this and other points. That will be for Ms. Athanasoulis and the Proposal Trustee to decide.

[134] Ms. Athanasoulis has provided sufficient foundational evidence to satisfy the court that, while it may be difficult, efforts should be made to value the Profit Share Claim. As previously directed, the parties shall arrange to attend before me on a case conference at which proposals will be made and directions will be provided regarding the process for the valuation of the Profit Share Claim.

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[6] The same may be true for the ongoing litigation that Ms. Athanasoulis has commenced against Mr. Casey regarding the alleged breaches of his fiduciary and other duties to attain, or at least maintain, the profitability of the YSL Project (and other Cresford Group projects) and to keep the YSL Project out of insolvency.

[135] At that case conference, directions may also be provided regarding any continued participation of the LPs, whose standing was granted for purposes of this stage because of unique perspectives that they might provide on the question of the validity or enforceability of the Profit Sharing Agreement (discussed later in this endorsement). It is not apparent that they have any unique perspective or entitlement to participate in the valuation of the Profit Share Claim, any more so than the other unsecured creditors who may also be impacted by that determination and who have not been granted standing. No standing arises merely from an economic interest in the outcome of the Proposal Trustee's determination (or valuation) of a proof of claim in these proceedings. See *YG Limited Partnership and YSL Residences Inc. (Re)*, 2023 ONCA 50, at para.19

Costs

[136] The parties have now uploaded their Bills of Costs or Costs Outlines referable to this appeal.

[137] All costs are presented on a partial indemnity basis. The amounts certified are as follows:

a. By the Proposal Trustee, $100,000 in fees (for approximately 157 lawyer hours, excluding the time of students and clerks) plus disbursements and applicable taxes, for a total of $114,745.85;

b. By the 250 LPs, approximately $62,927.21 in fees (for approximately 145 lawyer hours) inclusive of applicable taxes;

c. By the other LPs, $77,377.69 in fees (for approximately 190 lawyer hours), inclusive of applicable taxes;

d. By Ms. Athanasoulis, $193,612.50 in fees (for in excess of 400 lawyer hours) plus applicable disbursements and taxes, for a total of $231,057.19. By my estimation, approximately $24,000 of these fees claimed were for the earlier Jurisdiction Motion heard on October 17, 2022 and $13,000 of these fees claimed were for the Claims Procedure motion heard on January 16, 2023.

[138] At the hearing of the appeal, in the event that the court allows the appeal and sets aside the Disallowance the Proposal Trustee and LPs asked that any award of costs be deferred until after damages have been determined and the Profit Share Claim has been valued, on the premise that there still may be no, or a lower, amount attributed than has been claimed. It was also submitted that Ms. Athanasoulis should not be permitted to claim costs incurred for the earlier Jurisdiction and Claims Procedure motions.

[139] In that event, Ms. Athanasoulis asked for her costs to be fixed and ordered payable forthwith. She argues that this is consistent with the principles under r. 57 and that the only relevant prior costs ruling was that she was denied the right to claim costs thrown away relating to the work that had been done in respect of phase two of the Arbitration which the court ordered be terminated in the Funding Decision and replaced with this Claims Procedure.

[140] The total partial indemnity costs of Ms. Athanasoulis of just over $231,000 is just slightly less than the combined total costs of the Proposal Trustee and LPs of just over $240,000. The total lawyer hours are less for Ms. Athanasoulis compared to the aggregate lawyer hours on the opposing side. On that basis, there is no need for the court to get into a line-by-line review of the amounts claimed, hours spent or hourly rates. All parties were represented by excellent counsel who charged accordingly for their work. Ms. Athanasoulis had to address the arguments raised from all perspectives.

[141] Ms. Athanasoulis is a private individual who is funding this dispute regarding her Profit Share Claim herself. She was facing, as a result of the Disallowance, the complete loss of her $18 million Profit Share Claim. As a result of her success on this appeal she can now pursue that claim through the next valuation stage.

[142] The issues are important to Ms. Athanasoulis and to the other creditors of YSL from a financial perspective. She, also has reputational issues at stake. The private arbitration process that she and the Proposal Trustee had agreed to for the determination of the Athanasoulis Claims was derailed part way through as a result of objections raised by the Sponsor and the LPs, and through no fault of her own. While the bifurcation of the damages/valuation means there will be another stage, this stage dealing with the provability of the Profit Share Claim was decided in favour of Ms. Athanasoulis and she is entitled, as the successful party, to her partial indemnity costs as claimed.

[143] Costs associated with the damages/valuation stage will be separately determined and, if Ms. Athanasoulis is not successful at that stage, there may be cost consequences for her at that time. However, I do not agree that she should be deprived of any award of costs associated with this appeal and with the motion that determined the Claims Procedure that got the parties to this point. I do agree that the costs of the earlier Jurisdiction Motion (that resulted in the Funding Decision dealing with the Arbitration) should not be included and I have deducted those fees from the total partial indemnity fees that I am awarding to Ms. Athanasoulis, fixed in the amount of $169,715.93 plus applicable taxes and total disbursements of $6,812.08 (inclusive of HST).

[144] These costs have been determined in the exercise of my discretion under s. 131 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43 and with regard to the applicable factors under r. 57 of the *Rules of Civil Procedure*, R.R.O. 1990, Reg. 194, including those discussed above and the principles of proportionality and indemnity.

[145] I did not hear any submissions about whether these costs are sought only from the Proposal Trustee or if any party takes the position that some should be paid by the LPs. Unless there are submissions that any party wishes to make on that point (in which case, a case conference may be arranged to speak to this issue), I order the partial indemnity costs fixed at the amount of $169,715.93 plus applicable taxes and total disbursements of $6,812.08 (inclusive of HST) to be paid to Ms. Athanasoulis by the Proposal Trustee forthwith. If there are submissions to be made about the source of funds to be used by the Proposal Trustee to pay those costs, I may be spoken to about that as well.

Order and Final Disposition

[146] The following orders, declarations and directions are made or granted based on the relief requested in Ms. Athanasoulis' Notice of Motion on appeal:

a. The Proposal Trustee's Disallowance of the Profit Share Claim dated August 10, 2023 is set aside;

b. The Profit Share Claim is declared not to be an equity claim, and to be a provable claim within the meaning of s. 121(1) of the BIA;

c. The Profit Share Claim is entitled to priority over the claims asserted by the LPs;

d. Maria Athanasoulis' Profit Share Claim against YSL is declared to be a valid claim and ought to be allowed in an amount to be determined by further order of this court or by such other process as the court may direct;

e. Maria Athanasoulis shall be paid forthwith her partial indemnity costs of this motion/appeal from the Disallowance fixed in the amount of $169,715.93 plus applicable taxes and total disbursements of $6,812.08 (inclusive of HST), subject to further directions from the court to be provided at a case conference, if requested, regarding by whom, in what proportions and from what source these costs are to be paid;

f. The parties shall arrange a case conference before me for the purpose of making submissions and receiving directions regarding the process for the determination of the amount (valuation) of the Profit Share Claim. The Sponsor (or its counsel) shall also attend this case conference as it may have implications for the ongoing funding of administrative and other expenses of the Proposal Trustee associated with the determination of the Profit Share Claim;

g. The ongoing civil proceedings among and between Ms. Athanasoulis and the LPs and members of the Cresford Group may continue, subject only to the determinations herein regarding the validity, provability and priority of the Profit Share Claim.

[147] This endorsement and the orders, declarations and directions contained in it shall have the immediate effect of a court order without the necessity of a formal order being taken out, although any party may take out a formal order if so advised by following the procedure under r. 59.

Kimmel J.

Date: March 19, 2024

TAB 22

CITATION: Return on Innovation v. Gandi Innovations, 2011 ONSC 5018
COURT FILE NO.: 09-CL-8172
DATE: 20110825

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

B E T W E E N:

RETURN ON INNOVATION CAPITAL LTD. as agent for ROI FUND INC, ROI SCEPTRE CANADIAN RETIREMENT FUND, ROI GLOBAL RETIREMENT FUND and ROI HIGH YIELD PRIVATE PLACEMENT FUND and ANY OTHER FUND MANAGED BY ROI from time to time

Applicants

-and-

GANDI INNOVATIONS LIMITED, GANDI INNOVATIONS HOLDINGS LLC, GANDI INNOVATIONS LLC, GANDI INNOVATIONS HOLD CO AND GANDI SPECIAL HOLDINGS LLC.

Respondents

BEFORE: Justice Newbould

COUNSEL: Harvey Chaiton and Maya Poliak, for the Monitor, BDO Canada Limited

Mathew Halpin and Evan Cobb, for TA Associates Inc.

Christopher J. Cosgriffe, for Harry Gandy, James Gandy and Trent Garmoe

DATE HEARD: August 18, 2011

E N D O R S E M E N T

[1] This is a motion brought by BDO Canada Limited in its capacity as the Court-appointed Monitor of Gandi Innovations Limited, Gandi Innovations Holdings LLC, Gandi Innovations LLC, Gandi Innovations Hold Co, and Gandi Special Holdings LLC (the "Gandi Group") for advice and directions, and particularly to determine preliminary issues in connection with the

indemnity claims made by Hary Gandy, James Gandy and Trent Garmoe (the “Claimants”) against all of the Gandi Group.

[2] The Gandi Group is under CCAA protection. The Monitor was appointed in the Initial Order on May 8, 2009.

[3] The business and assets of the Gandi Group have been sold with court approval. The proceeds from the sale are being held by the Monitor for eventual distribution to unsecured creditors pursuant to a plan of compromise and arrangement.

Arbitration proceedings and indemnity claims

[4] Gandi Innovations Holdings LLC ("Gandi Holdings") was incorporated pursuant to the laws of the State of Delaware on August 24, 2007. On September 12, 2007, the Gandi Group re-organized their business structure so that Gandi Holdings became the direct or indirect parent of the other various entities comprising the Gandi Group.

[5] TA Associates Inc. is a general partner for a number of TA partners. In conjunction with the reorganization of Gandi Holdings, it advanced approximately US $75 million on September 12, 2007 by way of debt and equity to the Gandi Group. The advance consisted of:

> (i) an equity investment in the amount of US $50 million made pursuant to the terms of a Membership Interest Purchase Agreement in respect of Gandi Holdings dated as of September 12, 2007 made between, among others, Gandi Holdings, TA Associates and the Claimants in their personal capacities; and
>
> (ii) an unsecured loan in the amount of US $25 million which amount was guaranteed by other members of the Gandi Group.

[6] In January 2009, TA Associates commenced an arbitration proceeding against the Claimants. In the arbitration TA Associates claim damages against the Claimants in an amount of US $75 million with interest, being the total amount of TA Associates’ investment in the Gandi Group. The arbitration has not yet been heard on its merits.

[7] On December 20, 2010, the Monitor received proofs of claim of Hary Gandy and James Gandy against the Gandi Group in the approximate amount of $76 million and a proof of claim of Trent Garmoe against the Gandi Group in an approximate amount of $88 million. The Claimants assert an entitlement to indemnification by the Gandi Group in respect of any award of damages which may be made against them in the arbitration together with all legal fees incurred by the Claimants in defending the arbitration.

[8] The proofs of claim filed by the Claimants rely on indemnity provisions set out in the Amended and Restated Limited Liability Company Agreement of Gandi Holdings and a separate Indemnification Agreement made by Gandi Holdings entered into in connection with the Membership Agreement made at the time of the TA Associates investment with Gandi Holdings. Gandi Holdings is the only Gandi entity that is a party to these indemnity agreements.

[9] On March 11, 2011 the Monitor disallowed the indemnity claims and advised the Claimants that based on the evidence filed in support of the indemnity claims, any indemnity claim would be solely against Gandi Holdings.

[10] The Claimants have served notices of dispute and have provided to the Monitor a memorandum of articles of Association of Gandi Canada which provides an indemnity in favour of directors and officers of Gandi Canada in certain circumstances.

[11] There is also an indemnity of Gandi Innovations Hold Co ("Gandi Hold Co"). At the relevant times James Gandy was the sole director of the company.

[12] There has been an extensive search for corporate documents. The Monitor made inquiries of Jaffe Raitt Heuer & Weiss Inc., former corporate counsel of the Gandi Group, and learned that all of corporate governance documents of the Gandi Group, at Hary Gandy’s request, had been sent to Stikeman Elliot LLP, insolvency counsel for the Gandi Group, following the CCAA filing date. Counsel for the Monitor attended at the offices of Stikeman Elliott and reviewed the corporate governance documents in its possession.

[13] In addition the Monitor contacted counsel for Agfa, the purchaser of the assets of the Gandi Group, to inquire if it has in its possession copies of the Gandi Group's corporate governance records. The Monitor was advised by counsel for Agfa that Agfa was not able to find any corporate governance documents of the Gandi Group entities.

[14] The Monitor also reviewed the books and records of the Gandi Group in storage. In addition, the Monitor advised the Claimants that should they wish to undertake a review of the Gandi Group's records in storage, the Claimants were invited to contact the Monitor and arrange for such review. The review was arranged and conducted by the Claimants on June 3, 2011.

[15] It is a fact that there are not in existence documents that support the Claimants all being entitled to indemnities from each corporate entity in the Gaudi Group.

Issues

[16] Whether the Claimants will ever be with held liable in the arbitration is not yet known. However, whether the Claimants have rights to indemnification against all of the Gandi Group or against only Gandi Holdings and Gandi Hold Co will assist the Monitor in determining whether to proceed with a consolidated plan of arrangement or file an alternative plan excluding Gandi Holdings and/or Gandi Hold Co which would enable the Monitor to make a meaningful distribution to unsecured creditors prior to the completion of the arbitration.

[17] There is another preliminary issue. In the arbitration, TA Associates seeks to recover against the Claimants their equity investment of US $50 million, for which the Claimants in turn have sought indemnification from the Gandi Group. The Monitor seeks a preliminary determination as to whether these claims for indemnification relating to the claim by TA Associates for its equity investment constitute "equity claims" under the CCAA. A determination of this issue will assist the Monitor in determining the maximum amount which can be claimed by the Claimants and may facilitate an earlier distribution of funds available to unsecured creditors.

Discussion

(a) Indemnity agreements

[18] An Amended and Restated Limited Liability Company Agreement of Gandi Holdings dated September 12, 2007 provides for an indemnity by Gandi Holdings in section 6.8(a) for board members and officers. There is no dispute that the Claimants were officers and board members of Gandi Holdings. It also contains in section 7.6 an indemnity for Members as follows:

> (a) Without limitation of any other provision of this Agreement executed in connection herewith, the Company agrees to defend, indemnify and hold each Member, its affiliates and their respective direct and indirect partners (including partners of partners and stockholders and members of partners), members, stockholders, directors, officers, employees and agents and each person who controls any of them…

[19] Superwide Limited Partnership is a Member and the Claimants are partners of Superwide. Thus the Claimants are indemnified by Gandi Holdings by that provision as well.

[20] There is a form on indemnity agreement made between Gandi Holdings and indemnitees. The form in the record is an unsigned copy dated September 11, 2007. Neither the monitor nor any of the parties have been able to locate any of these agreements signed in favour of the Claimants. Hary Gandi, who swore an affidavit for the Claimants, said that a copy of this agreement was signed between Gandi Holdings and each of the Claimants on September 12, 2007. It contains the following:

> WHEREAS, the Company desires to provide Indemnitee with specific contractual assurance of Indemnitee's rights to full indemnification against litigation risks and related expenses (regardless, among other things, of any amendment to or revocation of the Company's LLC Agreement or any change in the ownership of the Company or the composition of its Board of Managers) . . .
> …
> 3. Agreement to indemnify… if Indemnitee was or is a party or is threatened to be made a party to any Proceeding by reason of Indemnitee's Corporate Status, Indemnitee shall be indemnified by the Company against all Expenses and Liabilities incurred . . . ."

[21] Assuming that this form of indemnity agreement was signed by Gandi Holdings and the Claimants, they would be covered by it.

[22] The Claimants contend that each of the corporate entities in the Gandi Group signed an indemnity in favour of each of them. This is based on a statement in the affidavit of Hary Gandy that Gandi Holdings and the other CCAA Respondents provided additional indemnities to him, James Gandy and Trent Garmoe dated September 12, 2007. He attached to his affidavit a form of the indemnification agreement to be signed by Gandi Holdings. No affidavit was filed from James Gandy or Trent Garmoe.

[23] There is no form of indemnity agreement in existence which names an indemnifier other than Gandi Holdings.

[24] The date of September 12, 2007, said to be the date that all of the entities in the Gandi Group signed indemnities in favour of each of the claimants, was the date of the investment by TA Associates in which it purchased a membership interest in Gandi Holdings only. Representatives of TA Associates received identical indemnities from Gandi Holdings. There is no evidence that any indemnities from any of the other Gandi Group entities were made at that time. To the contrary, the Membership Interest Purchase Agreement under which TA Associates purchased its membership interest in Gandi Holdings contained as a condition to closing a requirement that Gandi Holdings sign an indemnification agreement. The indemnification was only to be given by Gandi Holdings. There was no requirement for an indemnity to be given by any other entity in the Gandi Group,.

[25] I do not accept the bald statement of Hary Gandy that all of the entities in the Gandi Group gave indemnities at the time. The only indemnities that were given were by Gaudi Holdings.

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(b) Memorandum and articles of Gandi Hold Co

[26] In the course of its investigation, the Monitor did locate an indemnity granted by Gandi Hold Co in its Memorandum and Articles in favour of its directors and officers. Those articles contain an indemnity in the same terms as the indemnity in the Gandi Innovations Limited articles, as discussed below. As the Monitor does not seek a determination regarding indemnities

given by Gandi Hold Co, I need not discuss whether one or more of the Claimants is entitled to be indemnified by these articles.

(c) Articles of Association of Gandi Innovations Limited (Gandi Canada)

[27] The articles of this company contain an indemnity as follows:

> Every director or officer, former director or officer, or person who acts or acted at the Company's request**,** as a director or officer of the Company, a body corporate, partnership or other association of which the Company is or was a shareholder, partner, member or creditor and the heirs and legal representatives of such person, in absence of any dishonesty on the part of such persons shall be indemnified by the Company…in respect of any claim made against such person … by reason of being or having been a director or officer of the Company. [emphasis added]

[28] The corporate records sent to the Monitor by the corporate solicitors who incorporated the company name James Gandy as the president, treasurer and secretary and as the sole director. Hary Gandy stated at the outset of his affidavit filed on behalf of the claimants that he was the president and chief executive officer and chairman of the board of the companies that made up the Gandi Group. There are no corporate records that support that assertion and on his cross-examination he acknowledged he had no documents, including board resolutions, contracts or appointment letters to show that he was ever a director or officer of Gandi Innovations Limited. He said that he was directing the business of all of the entities. On his cross-examination, he said that as far as he was concerned, James Handy and Trent Garmoe were directors and officers of the company.

[29] James Gandy did not file any affidavit to say that he was not the president, treasurer and secretary of the company, as shown in the corporate records. Trent Garmoe did not file any affidavit. I think it fair to draw an adverse inference that their evidence would not have been helpful to their case.

[30] The affidavit of Bruce Johnston filed on behalf of TA Associates states that Hary Gandy and Trent Garmoe were not directors or officers of Gandi Innovations Limited and that a document printed from the Nova Scotia Registry of Joint Stock Companies which was included

in the closing documents for TA Associates' investment showed that James Gandy was the only director and officer of Gandi Innovations Limited.

[31] There has been an extensive search for corporate documents but none have been found that would support Hary Gundy or Trent Garmoe as being an officer or director of Gandi Innovations Limited.

[32] It is argued that the indemnity in the articles of Gandi Innovations Limited is in favour not only of officers and directors, but also "persons who acted at the Company's request as a director or officer of the Company", and that Hary Gandy and Trent Garmoe acted as directors and officers at the Company's request. There is certainly no documentary evidence of that. Presumably the request would have had to come from James Gandy, who is the sole officer and director according to the corporate records. There is no evidence from any of the Claimants that any request was made to Hary Gandy or Trent Garmoe to act as an officer or director of Gandi Innovations Limited, which one would have expected if the assertion was to be made.

[33] It is also argued that the board of managers (the Delaware concept of a board of directors) of Gandi Holdings operated the subsidiaries as if they were officers and directors of the subsidiaries. Again, there is no documentary evidence of that and no evidence from any of the Claimants to support the assertion. While Hary Gandy may have operated the business in a functional sense, that does not mean that he was acting as an officer or director of any subsidiary in the corporate sense. This is not mere semantics. TA Associates made a large investment, and one of the corporate documents provided on closing was the Nova Scotia Registry of Joint Stock Companies that showed only James Gandy as an officer and director. If all of the Claimants are entitled to be indemnified by Gandi Innovations Limited, it will impact the claim of TA Associates in the CCAA proceedings.

[34] In the circumstances, I find that the only person entitled to indemnification from Gandi Innovations Limited is James Gandy.

[35] However, in connection with the financing provided by TA Associates, James Gandy executed a Subordination Agreement dated as of September, 12, 2007 under which he agreed

that any liability or obligations of Gandi Canada to him, present or in the future, would be deferred, postponed and subordinated in all respects to the repayment in full by Gandi Innovations of all indebtedness, liabilities and obligations owing to TA Associates in connection with the purchase by TA Associates of US $25million in notes. Until that obligation to pay the notes in full with interest has been fulfilled, any claim by James Gandy under the indemnity from Gandi Innovations Limited is subordinated to the claim of TA Associates.

[36] The debt claim of TA Associates of $46,733,145 has been accepted by the Monitor. Assuming that the purchase price on the sale of the assets to Agfa is received in full, the monitor expects a distribution to unsecured creditors of approximately 27% of the value of their claims. In such circumstances, James Gundy will have no right to receive any payment from Gandi Innovations Limited in respect of his indemnity claim.

(d) Other Gaudi Group entities

[37] It was asserted by the Claimants that because the Gandi companies operated essentially as one integrated company, it should be inferred that the constating documents of the other entities in the Gandi Group contained the same indemnity as contained in the bylaws of Gandi Innovations Limited and Gandi Hold Co. I do not agree.

[38] Gandi Innovations LLC is a Texas company. Its Amended and Restated Operating Agreement contains the types of things normally contained in a general bylaw of an Ontario corporation. It contains no provision for indemnities. It was argued that as no articles were obtained from Texas, it could be assumed that the articles contained an indemnity provision similar to that contained in the bylaws of Gandi Innovations Limited and Gandi Hold Co. I asked counsel to obtain whatever documentation was available in Texas, and subsequently the Monitor received from its US counsel, Vinson & Elkins LLP, a copy of articles of organization for Gandi Innovations LLC dated August 2, 2004. There is nothing in these articles dealing with indemnities. Vinson & Elkins LLP advised that these articles, together with amending articles already in the possession of the Monitor, are the only corporate governance documents on file with the State of Texas.

[39] Gandi Special Holdings LLC is a Delaware corporation. The Limited Liability Company Agreement of Gandi Special Holdings LLC, like the Texas company, contains the types of things normally contained in a general bylaw of an Ontario corporation. It contains no provision for indemnities. Following the hearing, the Monitor obtained through Vinson & Elkins LLP a Delaware Certificate of Formation of Gandi Special Holdings LLC. This document contains no provision for indemnities. A certificate of the Secretary of State of Delaware confirms that there were no other relevant documents on file and this was confirmed by Vinson & Elkins LLP.

[40] I find that there is no indemnity in favour of the Claimants in the corporate documentation of Gandi Innovations LLC and Gandi Special Holdings LLC.

[41] It is also argued on behalf of the Claimants that the Gandi Group have acknowledged an obligation to indemnify the Claimants and it is said that this arises from a meeting of the board of Gandi Holdings. It is argued that the Gandi Group through the Monitor is thus estopped from denying an indemnity for all of the Gandi Group companies. A document said to be minutes of a meeting of the board of managers of Gandi Holdings held on March 4, 2009 is relied on. That document contains the following paragraph:

> The next item on the agenda was the indemnification of the officers. It was generally agreed that all parties would follow the Purchase Agreement between Gandi Innovations and TA Resources dated September 12, 2007: Counsel for TA had previously expressed the opinion that indemnification was not allowed under the purchase agreement. Counsel for James Gandy, Hary Gandy and Trent Garmoe together with the Corporate Counsel, Matthew Murphy had previously expressed verbal opinions that the indemnification of the officers was permitted under the Purchase Agreement. Lydia Garay, as the only member not involved in the dispute between TA and the key holders, voted to follow the advice of Corporate Counsel, Matthew Murphy. To avoid any misunderstanding, Corporate Counsel would be requested to express that opinion in writing.

[42] I do not see this paragraph in the informal minutes as assisting the Claimants. It is a meeting of the board of Gandi Holdings. It says that it was generally agreed that all parties would follow the purchase agreement between Gandi Holdings and TA resources dated September 12, 2007. That purchase agreement provides for an indemnity by only Gandi Holdings. Assuming that the minutes reflect a desire of some board members to indemnify officers of subsidiary

corporations, and assuming that the Claimants thought they were officers of all of the subsidiary corporations, it is quite clear from the paragraph that there was a difference of view. The minute states that counsel for TA Associates had previously expressed the opinion that indemnification was not allowed under the purchase agreement and that counsel for the Claimants together with corporate counsel, Matthew Murphy, expressed the opposite opinion. The minute states that Lydia Garay, the only member not involved in the dispute between TA Associates and the key holders, voted to follow the advice of Corporate Counsel Terry Murphy and to avoid any misunderstanding, corporate counsel would be requested to express that opinion in writing.

[43] The affidavit of Bruce Johnston on behalf of TA Associates, who attended that meeting of the board of managers of Gandi Holdings swears that the Claimants voted to place Lydia Garay, a longtime employee and officer of Gandi Holdings, on the board despite a verbal agreement that he had with the Claimants to leave that board seat vacant and to work with him to appoint an outside independent board member. He stated Ms. Garay was completely reliant on the Gandy family for her job security and compensation.

[44] Mr. Johnston also states in his affidavit that the indemnification of the Claimants was discussed and that he and Mr. Taylor took the position that indemnification was not permitted. He said the Claimants took the position that indemnification was permitted, despite the language of the purchase agreement, and took the position that corporate counsel for Gandi Holdings had previously given a verbal opinion that indemnification was permitted under the purchase agreement. After hearing that, and during the meeting, Mr. Johnston sent an e-mail to Mr. Murphy who two minutes later responded that he had not advised on the question of an indemnity under the purchase agreement. Mr. Johnson states that he then read that e-mail at the meeting. I accept his evidence on this.

[45] Whether or not Ms. Garay was a disinterested or proper member of the board of management of Gandi Holdings, the minute states that she voted to follow the advice of corporate counsel. At the next board meeting on May 4, 2009, Ms. Garay said that she had sought the written opinion of corporate counsel but had not received it. To date no opinion from Mr. Murphy has surfaced. On the face of those minutes from March 4, 2009, there has been no

approval of any indemnities in favour of the Claimants for other corporations. I cannot find on the evidence that there was any agreement that the Claimants would be indemnified by subsidiary corporations, nor is there any evidence that any subsidiary corporation ever enacted any documentation of any kind to provide such indemnities. The opposite is the case, as has been discussed.

[46] Finally, the Claimants allege that the Gandi Group has previously acknowledged their liability to indemnify the Claimants for any damage, award or legal costs incurred by the following actions:

(i) certain Gandi entities made payments of defence costs in connection with the arbitration both pre-and post the CCAA filing; and
(ii) the Monitor allegedly approved payment of post-filing defence costs.

[47] Until the sale of the Gandi Group to Agfa was completed, this CCAA proceeding was a debtor in possession restructuring with the business and affairs of the Gandi Group being managed by their officers and directors, specifically Hary Gundy and Trent Garmoe. Payments of legal fees to Langley and Banack Inc., U.S. lawyers for the Gandi Group and the Claimants, were made by or on authorization of Trent Garmoe.

[48] Pursuant to the terms of the Initial Order, the Monitor was required to approve all expenditures over $10,000 before payment was made. The Monitor approved payment of legal fees to counsel for the Gandi Group on the general understanding that such fees were incurred by the Gandi Group in connection with the Gandi Group's insolvency proceeding and for general corporate work for the Gandi Group.

[49] I accept the statement of the Monitor that it did not knowingly approve the payment of the Claimants' defence costs in connection with the arbitration.

[50] Subsequent to the completion of the sale to Agfa, the Monitor learned that a nominal amount of the legal fees approved by the Monitor was subsequently allocated to cover the costs of the arbitration. I accept the statement of the Monitor that it had no input, knowledge or control

over such allocation, and had it been consulted, would have been opposed to such allocation as it did not involve any member of the Gandi Group.

[51] In the circumstances there is no basis for the assertion that the Monitor is somehow estopped by reason of the payment of legal fees from denying that there are other indemnities in favour of the Claimants.

(e) Are the Claimants claims debt or equity claims?

[52] This involves the application of provisions of the CCAA to the claims asserted by TA Associates in the arbitration.

[53] Section 6(8) of the CCAA provides:

> No compromise or arrangement that provides for the payment of an equity claim is to be sanctioned by the court unless it provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid.

[54] In s. 2(1) of the CCAA, equity claims are defined as follows:

> "equity claim" means a claim that is in respect of an equity interest, including a claim for, among others,
> (a) a dividend or similar payment,
> (b) a return of capital,
> (c) a redemption or retraction obligation,
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);

[55] This definition of equity claim came into force on September 18, 2009. Although this provision does not apply to the Gandi Group's CCAA proceedings which commenced shortly prior to the legislative amendments, courts have noted that the amendments codified existing

case law relating to the treatment of equity claims in insolvency proceedings. In *Re Nelson Financial Group Lrd*., (2010) 75 B.L.R. (4th) 302, Pepall J. stated:

> The amendments to the CCAA came into force on September 18, 2009. It is clear that the amendments incorporated the historical treatment of equity claims. The language of section 2 is clear and broad. Equity claim means a claim in respect of an equity interest and includes, amongst other things, a claim for rescission of a purchase or sale of an equity interest. Pursuant to sections 6(8) and 22.1, equity claims are rendered subordinate to those of creditors.
>
> ,

[56] If the claims in the arbitration commenced by TA Associates against the Claimants are equity claims, the claims by the Claimants in the CCAA process for contribution or indemnity in respect of those claims would be equity claims. The Claimants contend that the claims in the arbitration are not equity claims.

[57] The claims in the arbitration by TA Associates against the creditors include claims for various breaches of contract, fraud, rescission, or in the alternative, recissory damages, negligent misrepresentation, breach of fiduciary duty and tortious interference with advantageous business relationships and prospective economic advantage.

[58] In the arbitration TA Associates seeks to recover the investment that it made in Gandi Holdings, including the US $25 million debt secured by promissory notes and the US $50 million equity investment made by way of a membership subscription in Gandi Holdings.

[59] The Claimants assert that the claim for US $50 million by TA Associates cannot be an equity claim because it is based on breaches of contract, torts and equity. I do not see that as being the deciding factor. TA Associates seeks the return of its US $50 million equity investment because of various wrongdoings alleged against the Claimants and the fact that the claim is based on these causes of action does not make it any less a claim in equity. The legal tools that are used is not the important thing. It is the fact that they are being used to recover an equity investment that is important.

[60] In *Re Nelson Financial Group Lrd.*, *supra*, at Peppall J. stated that historically, the claims and rights of shareholders were not treated as provable claims and ranked after creditors of an insolvent corporation in a liquidation. She also stated:

> This treatment also has been held to encompass fraudulent misrepresentation claims advanced by a shareholder seeking to recover his investment: *Re Blue Range Resource Corp.*In that case, Romaine J. held that the alleged loss derived from and was inextricably intertwined with the shareholder interest. Similarly, in the United States, the Second Circuit Court of Appeal in *Re Stirling Homex Corp*. concluded that shareholders, including those who had allegedly been defrauded, were subordinate to the general creditors when the company was insolvent.

[61] As the amendments to the CCAA incorporated the historical treatment of equity claims, in my view the claims of TA Associates in the arbitration to be compensated for the loss of its equity interest of US $50 million is to be treated as an equity claim and that the claims of the Claimants for indemnity against that claim is also to be treated as an equity claim in this CCAA proceeding.

Order

[62] An order in the form of a declaration shall go in accordance with these reasons.

._____

Newbould J.

DATE: August 25, 2011

TAB 23

Schnier v. The Attorney General of Canada
[Indexed as: Schnier v. Canada (Attorney General)]

Ontario Reports

Court of Appeal for Ontario,

Gillese, Blair and D.M. Brown JJ.A.

January 6, 2016

128 O.R. (3d) 537 | 2016 ONCA 5

Case Summary

Bankruptcy and insolvency — Discharge — Personal income tax debt — Amount of assessed personal income tax that was under appeal at time of bankrupt's discharge hearing not included in calculating bankrupt's personal income tax debt under s. 172.1(1) of Bankruptcy and Insolvency Act — Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, s. 172.1(1). [page538]

At the time of the bankrupt's discharge, he had unpaid income tax assessments totalling approximately $4.478 million. About $4.424 million of that amount was subject to outstanding appeals by the bankrupt to the Tax Court of Canada. If the full assessed amount was considered part of his personal income tax debt, s. 172.1 of the Bankruptcy and Insolvency Act would apply to his bankruptcy; if the appealed amounts were excluded, s. 172.1 would not apply. The registrar in bankruptcy held that s. 172.1 did not apply to the discharge application. She discharged the bankrupt, subject to a condition that he remit to the trustee the remaining surplus income payable, up to a maximum of $10,000. The motion judge dismissed the Attorney General's motion by way of appeal. The Attorney General appealed.

Held, the appeal should be dismissed.

In calculating the bankrupt's personal income tax debt under s. 172.1(1) of the Bankruptcy and Insolvency Act, the assessed amounts of personal income tax that were under appeal at the time of his discharge hearing were not to be included. The motion judge and the registrar correctly concluded that until the Tax Court of Canada had disposed of the bankrupt's appeals of the assessments, the portion of the Canada Revenue Agency's claim for the assessed amounts under appeal was a contingent one that the trustee could refuse to admit as a proven claim. The stipulation in s. 158 of the Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.) that any unpaid amount assessed is "payable forthwith" upon the mailing of a notice of assessment must be understood within the larger context of the taxpayer's right under the Income Tax Act to object to an assessment and to appeal a minister's confirmation of an assessment to the Tax Court of Canada.

2713250 Canada inc. (Re), [2011] J.Q. no 16993, 2011 QCCS 6119, 2012EXP-83, J.E. 2012-61, EYB 2011-198510, 86 C.B.R. (5th) 204; Norris (Re) (1989), 69 O.R. (2d) 285, [1989] O.J.

No. 995, 60 D.L.R. (4th) 606, 34 O.A.C. 304, 75 C.B.R. (N.S.) 97, [1989] 2 C.T.C. 185, 89 D.T.C. 5493, 16 A.C.W.S. (3d) 161 (C.A.); Port Chevrolet Oldsmobile Ltd. (Re), [2004] B.C.J. No. 101, 2004 BCCA 37, 193 B.C.A.C. 114, 23 B.C.L.R. (4th) 335, 49 C.B.R. (4th) 146, [2004] G.S.T.C. 8, 128 A.C.W.S. (3d) 436, affg [2002] B.C.J. No. 3206, 2002 BCSC 1874, 49 C.B.R. (4th) 127, [2003] G.S.T.C. 168, consd

Other cases referred to

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Leung v. Canada, [1993] F.C.J. No. 942, [1994] 1 F.C. 482, 67 F.T.R. 1, [1993] 2 C.T.C. 284, 93 D.T.C. 5467, 42 A.C.W.S. (3d) 1104 (T.D.); Murphy v. Sally Creek Environs Corp. (Trustee of), [2010] O.J. No. 1773, 2010 ONCA 312, 261 O.A.C. 199, 67 C.B.R. (5th) 161, 188 A.C.W.S. (3d) 344; Newfoundland and Labrador v. AbitibiBowater Inc., [2012] 3 S.C.R. 443, [2012] S.C.J. No. 67, 2012 SCC 67, 438 N.R. 134, 2012EXP-4268, J.E. 2012-2270, EYB 2012-215017, 352 D.L.R. (4th) 399, 95 C.B.R. (5th) 200, 71 C.E.L.R. (3d) 1, 221 A.C.W.S. (3d) 264; Regina Shoppers Mall Ltd. v. Canada, [1991] F.C.J. No. 52, 126 N.R. 141, [1991] 1 C.T.C. 297, 91 D.T.C. 5101, 25 A.C.W.S. (3d) 748 (C.A.); Rizzo & Rizzo Shoes Ltd. (Re) (1998), 36 O.R. (3d) 418, [1998] 1 S.C.R. 27, [1998] S.C.J. No. 2, 154 D.L.R. (4th) 193, 221 N.R. 241, J.E. 98-201, 106 O.A.C. 1, 50 C.B.R. (3d) 163, 33 C.C.E.L. (2d) 173, 98 CLLC Â210-006, D.T.E. 98T-154, 76 A.C.W.S. (3d) 894; Royal Bank of Canada v. Central Capital Corp. (1996), 27 O.R. (3d) 494, [1996] O.J. No. 359, 132 D.L.R. (4th) 223, 88 O.A.C. 161, 26 B.L.R. (2d) 88, 38 C.B.R. (3d) 1, 61 A.C.W.S. (3d) 18 (C.A.); Terra Nova Properties Ltd. v. M.N.R., [1967] 2 Ex. C.R. 46, [1967] C.T.C. 82, 67 D.T.C. 5064 (Exch. Ct.); Wesbrook Management Ltd. v. Canada, [1996] F.C.J. No. 1466, 206 N.R. 23, [1997] 1 C.T.C. 124, 96 D.T.C. 6590, 67 A.C.W.S. (3d) 191 (C.A.) [page539]

Statutes referred to

Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, ss. 108 [as am.], (1) [as am.], 121 [as am.], (1), (2) [as am.], 135 [as am.], (1.1) [as am.], (3) [as am.], 136(1) [as am.], 170(1) [as am.], 172.1 [as am.], (1), (8) [as am.]

Excise Tax Act, R.S.C. 1985, c. E-15 [as am.]

Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.) [as am.], ss. 152(8) [as am.], 158 [as am.], 165(3) [as am.], Part XV [as am.], ss. 223(1) [as am.], (2), 223-225 [as am.], 225.1 [as am.], (2) [as am.], (3) [as am.], (5) [as am.], 225.2, 248(2) [as am.]

APPEAL from the order of T.J. McEwen J. of the Superior Court of Justice dated December 8, 2014 affirming a decision of the registrar in bankruptcy.

Kevin Dias and Maria Vujnovic, for appellant.

Fred Tayar, for respondent.

The judgment of the court was delivered by

D.M. BROWN J.A.: —

I. Overview

[1] Special rules govern discharge hearings in income tax-driven personal bankruptcies. Section 172.1 of the Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3 ("BIA") provides that where the bankrupt has $200,000 or more of personal income tax debt and that personal income tax debt represents 75 per cent or more of the bankrupt's total unsecured proven claims, the timing of the discharge hearing, the discharge orders available to the court to make, and the factors the court must take into account in deciding the discharge application differ from those applied in a standard bankruptcy.

[2] At the time of his discharge hearing, the respondent bankrupt, Paul Schnier, had unpaid income tax assessments totalling approximately $4.478 million. About $4.424 million of that amount was subject to outstanding appeals he had filed in the Tax Court of Canada. If the full assessed amount was considered part of his personal income tax debt, s. 172.1 of the BIA would apply to his bankruptcy; if the appealed amounts were excluded, s. 172.1 would not apply.

[3] The registrar in bankruptcy held that s. 172.1 of the BIA did not apply to Mr. Schnier's application for discharge. Her order of July 18, 2014 (the "discharge order") discharged Mr. Schnier, subject to the condition that he remit to the trustee the remaining surplus income payable, up to a maximum of $10,000. [page540]

[4] By order dated December 8, 2014 (the "appeal order"), the motion judge dismissed the Attorney General's motion by way of appeal from the discharge order. The Attorney General now appeals to this court.

[5] Although the Attorney General asks that the appeal order be set aside, if it is, the Attorney General does not seek to vary the conditions of the discharge order made by the registrar. The relief sought by the Attorney General on this appeal is limited to a determination that s. 172.1 of the BIA applied to Mr. Schnier's discharge hearing.

[6] The issue then, on this appeal, is a narrow one: In calculating Mr. Schnier's personal income tax debt under BIA, s. 172.1(1), should the assessed amounts of personal income tax that were under appeal at the time of his discharge hearing be included?

[7] For the reasons set out below, I conclude the answer is no, and I would dismiss the appeal. Both the motion judge and the registrar correctly concluded that until the Tax Court of Canada had disposed of Mr. Schnier's appeals of the Canada Revenue Agency ("CRA") assessments, the portion of the CRA's claim for the assessed amounts under appeal was a contingent one that the trustee could refuse to admit as a proven claim. Accordingly, the motion judge and the registrar correctly held that s. 172.1 of the BIA did not apply to Mr. Schnier's

discharge hearing.

II. Background

[8] Mr. Schnier is a tax lawyer. His bankruptcy was driven by investments he made in two types of tax shelters. Between 1985 and 1991, Mr. Schnier invested in two yacht tax shelters. In the 1990s and early 2000s, he invested in four computer software tax shelters. Mr. Schnier claimed deductions from his income on those investments for either interest expenses or business losses. At the time Mr. Schnier made these investments, he believed that the tax shelters were permitted under the Income Tax Act, R.S.C. 1985, c. 1 (5th Supp.) ("ITA"); he had made the investments after receiving opinions from independent tax lawyers and accountants.

[9] Beginning in 1989, Mr. Schnier received notices of reassessment in relation to the yacht tax shelters going back to the 1985 taxation year. He immediately served on the Minister of National Revenue notices of objection to all of the CRA reassessments.

[10] Section 165(3) of the ITA provides that upon receipt of a notice of objection, the minister "shall, with all due dispatch, reconsider the assessment and vacate, confirm or vary the [page541] assessment or reassess". That did not occur in this case. Inexplicably, the minister allowed Mr. Schnier's objections to languish for over two decades. During that time, Mr. Schnier repeatedly asked the CRA to deal with his file, to no avail. It was not until October 2011 that the minister confirmed the reassessments for the yacht tax shelters. Mr. Schnier promptly filed notices of appeal to the Tax Court of Canada in November 2011.

[11] The following month, Mr. Schnier made a proposal to his creditors under the BIA. At that time, he had been assessed $1,278,519.62 in income tax, plus penalties and interest, for a total of $4,478,703.19. Although Mr. Schnier increased the amount of his proposal to creditors over the course of the following creditors' meetings, the CRA rejected the proposal, resulting in his deemed assignment into bankruptcy on January 19, 2012.

[12] On February 1, 2012, the CRA filed a proof of claim in the bankruptcy in the amount of $4,478,703.19 (the "claim"). The CRA disclosed that of the amount claimed, $4,424,558.19 was under appeal.

[13] In January 2013, the minister confirmed the assessments for the computer software tax shelters. Mr. Schnier filed appeals from those assessments in April 2013.

[14] In its February 4, 2014 report on the bankrupt's application for discharge, the trustee noted that the Tax Court had not yet determined Mr. Schnier's appeals of the CRA assessments. As a result, the trustee reported that it was "unable to value the claim and has not admitted CRA's claim for the assessed amounts under appeal as it is contingent". Consequently, the trustee's July 9, 2014 claims register admitted only $71,170.40 of the claim, and recorded the remaining $4.424 million of the claim as a contingent claim which was not admitted by the trustee.

[15] The CRA opposed Mr. Schnier's application to be discharged from bankruptcy.

[16] The registrar was required to consider whether the rules governing tax-driven personal bankruptcies set out in BIA, s. 172.1 applied to Mr. Schnier's bankruptcy. The reason is that important differences exist in the discharge procedures for individual bankrupts who fall within s.

172.1 and those who do not:

(i) in a standard personal bankruptcy, the passage of time may result in the automatic discharge of a bankrupt; under s. 172.1, an application to the court for a discharge hearing must be made;

(ii) in a standard personal bankruptcy, the court may grant an absolute order of discharge; such an order is not available if s. 172.1 applies; [page542]

(iii) if a court suspends the discharge in a s. 172.1 bankruptcy, the court must require the bankrupt to file income and expense statements with the trustee each month and to file all returns of income required by law to be filed; and

(iv) a court must take into account the following factors in considering a s. 172.1 discharge application: the circumstances of the bankrupt at the time the personal income tax debt was incurred; the efforts, if any, made by the bankrupt to pay the personal income tax debt; whether the bankrupt made payments in respect of other debts while failing to make reasonable efforts to pay the personal income tax debt; and the bankrupt's financial prospects.

[17] In her July 18, 2014 reasons, the registrar considered that the CRA was a proven creditor to the extent of the claims admitted by the trustee -- about $71,170. The balance of the CRA's claim consisted of assessed amounts of tax that were subject to appeals pending in the Tax Court of Canada and constituted a contingent claim. The registrar concluded that, "at present, the CRA has a contingent liability that cannot support the applicability of s. 172.1 of the BIA". On appeal, the motion judge agreed with the registrar.

III. Issue on the Appeal

[18] At issue on this appeal is whether s. 172.1(1) of the BIA applied to Mr. Schnier's discharge hearing. The section provides that the special income tax-driven bankruptcy discharge rules apply "[i]n the case of a bankrupt who has $200,000 or more of personal income tax debt and whose personal income tax debt represents 75% or more of the bankrupt's total unsecured proven claims".

[19] The parties offer competing interpretations of what constitutes "personal income tax debt" for purposes of s. 172.1. The Attorney General argues that "personal income tax debt" includes unpaid assessed tax, notwithstanding any right the taxpayer has to file an objection or appeal. The Attorney General submits that in this case, all of the $4.4 million CRA claimed in its proof of claim were amounts payable as of the dates of assessment, and remained payable under the ITA notwithstanding Mr. Schnier's subsequent appeals.

[20] The Attorney General submits that its interpretation is consistent with the express language of the ITA, which I discuss in detail below. It acknowledges a pair of cases that take the contrary view: [page543] Port Chevrolet Oldsmobile Ltd. (Re), [2002] B.C.J. No. 3206, 2002 BCSC 1874, 49 C.B.R. (4th) 127, affd [2004] B.C.J. No. 101, 2004 BCCA 37; and 2713250 Canada inc. (Re), [2011] J.Q. no 16993, 2011 QCCS 6119. The Attorney General submits that those cases were wrongly decided and should not be followed by this court.

[21] For his part, Mr. Schnier argues that on a proper interpretation of the ITA, his unpaid assessed amounts of tax that were subject to appeal were contingent claims which the trustee in bankruptcy did not accept as proven claims and, therefore, did not constitute "personal income tax debt" for the purposes of BIA, s. 172.1(1). Mr. Schnier submits that Port Chevrolet (Re) and 2713250 Canada inc. (Re) were correctly decided and should be followed by this court.

IV. Standard of Review

[22] The applicable standard of review was set out by this court in Murphy v. Sally Creek Environs Corp. (Trustee of), [2010] O.J. No. 1773, 2010 ONCA 312, 67 C.B.R. (5th) 161, at paras. 68, 70 and 72. On an appeal of a discharge order made by a registrar in bankruptcy, the reviewing motion judge may only set aside the order if the registrar erred in principle or in law, failed to take into account a proper factor, took into account an improper factor that demonstrably led to a wrong conclusion, or made a palpable and overriding error in respect of a finding of fact. The same standard of review applies to a further appeal to this court, although the decision under appeal is that of the motion judge, not the registrar. A motion judge will commit an error of law if he or she does not adhere to the correct standard when reviewing the registrar's decision.

V. Analysis

[23] Since the issue on this appeal concerns the interpretation of a statutory provision, I start by considering the legislative context in which s. 172.1 of the BIA is situated. I then outline and analyze the Attorney General's arguments regarding the proper interpretation of "personal income tax debt" that draw upon the language of the ITA. Next, I consider the Attorney General's argument that this court should decline to follow Port Chevrolet (Re) and 2713250 Canada inc. (Re). I then address the Attorney General's concern that upholding the motion judge's decision could invite abuse of the bankruptcy process. Finally, I consider the Attorney General's argument that the trustee in this case failed to determine whether or not CRA's claim was provable. [page544]

A. The legislative context for the analysis

[24] Applying the basic principle of statutory interpretation, the words "personal income tax debt" in BIA, s. 172.1(1) must be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the BIA, its object and the intention of Parliament: Rizzo & Rizzo Shoes Ltd. (Re) (1998), 36 O.R. (3d) 418, [1998] 1 S.C.R. 27, [1998] S.C.J. No. 2, at para. 21.

[25] A bankruptcy under the BIA follows a single proceeding model. In general terms, the property of the bankrupt not subject to security interests is realized and collected by the trustee in bankruptcy and then distributed to creditors with proven claims in accordance with the priorities set out in the scheme of distribution found in BIA, s. 136(1).

[26] At the heart of this distribution scheme lies the concept of creditor claims provable in bankruptcy. Section 121(1) of the BIA describes what claims are provable in a bankruptcy:

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

[27] Liquidated claims are not the only ones provable in a bankruptcy. Section 121(2) of the BIA specifically recognizes contingent claims as provable in a bankruptcy by providing that "[t]he determination whether a contingent or unliquidated claim is a provable claim and the valuation of such a claim shall be made in accordance with section 135".

[28] In each bankruptcy, the trustee must examine and classify the claims filed by the bankrupt's creditors: BIA, s. 135. As part of that process, the trustee must consider whether the characteristics of a debt claimed by a creditor are those of a liquidated claim, future claim or contingent claim. If a trustee concludes that the debt claimed has the character of a contingent claim, the trustee must then determine whether the contingent claim is a provable claim. As BIA, s. 135(1.1) states:

> 135(1.1) The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.

[29] As explained by the Supreme Court of Canada in Newfoundland and Labrador v. AbitibiBowater Inc., [2012] 3 S.C.R. 443, [2012] S.C.J. No. 67, 2012 SCC 67, at paras. 34 and 36, [page545] "a claim may be asserted in insolvency proceedings even if it is contingent on an event that has not yet occurred", and "[t]he criterion used by courts to determine whether a contingent claim will be included in the insolvency process is whether the event that has not yet occurred is too remote or speculative".

[30] This general legislative scheme for the examination and determination of creditor claims in a bankruptcy provides the critical context in which to determine the narrow issue raised by this appeal -- i.e., whether the assessed amounts of income tax that were under appeal at the time of Mr. Schnier's discharge hearing should be included when calculating his personal income tax debt under BIA, s. 172.1(1). That is so because whether s. 172.1 applies to a bankruptcy turns on how the trustee classifies a claim by the CRA for the payment of assessed amounts of income tax which remain subject to an appeal by the bankrupt taxpayer at the time of his discharge hearing. The arguments advanced by the parties about the proper interpretation of "personal income tax debt" in s. 172.1(1) must be assessed within the larger context of this legislative scheme.

B. "Amounts payable" within the meaning of ITA, s. 223(1)

[31] As noted, s. 172.1(1) of the BIA provides that the special discharge hearing rules apply "[i]n the case of a bankrupt who has $200,000 or more of personal income tax debt and whose personal income tax debt represents 75% or more of the bankrupt's total unsecured proven claims".

[32] Section 172.1(8) of the BIA defines "personal income tax debt" to mean "the amount payable, within the meaning of subsection 223(1) of the Income Tax Act . . . by an individual".

[33] Section 223(1) of the ITA defines an "amount payable" by a person as any or all of "an amount payable under this Act by the person".

[34] What are the fundamental characteristics of an "amount payable" under the ITA? The Attorney General argues that there are two. First, s. 158 of the ITA provides:

> 158. Where the Minister mails a notice of assessment of any amount payable by a taxpayer, that part of the amount assessed then remaining unpaid is payable forthwith by the taxpayer to the Receiver General.

[35] Second, s. 152(8) of the ITA deems an assessment to be "valid and binding". According to the Attorney General, when combined together these two characteristics of an unpaid assessed personal income tax debt are determinative of the analysis in this appeal. Even if a taxpayer appeals an assessment, the character of the tax debt remains one that is "payable [page546] forthwith" (s. 158) and "valid and binding" (s. 152(8)): in effect, a liquidated claim. As a result, the Attorney General submits, "personal income tax debt" within the meaning of BIA, s. 172.1(1) includes unpaid assessed amounts of income tax that are under appeal.

[36] I do not find that argument persuasive, for two reasons.

[37] First, the roles played by ss. 152(8) and 158 of the ITA in the characterization of an assessed tax debt must take into account the right of a taxpayer to appeal a notice of assessment to the Tax Court of Canada under Part I, Division J of the ITA.

[38] Section 152(8) of the ITA expressly provides that the valid and binding effect of an assessment is made subject to a taxpayer's right to appeal an assessment. The section states:

> 152(8) An assessment shall, subject to being varied or vacated on an objection or appeal under this Part and subject to a reassessment, be deemed to be valid and binding notwithstanding any error, defect or omission in the assessment or in any proceeding under this Act relating thereto.

(Emphasis added)

[39] As put by the Federal Court of Appeal in Wesbrook Management Ltd. v. Canada, [1996] F.C.J. No. 1466, [1997] 1 C.T.C. 124 (C.A.), at p. 129 C.T.C., when commenting on the effect of what is now s. 152(8): "Once . . . an assessment can no longer be varied or vacated on objection or appeal . . . the last assessment is deemed valid and binding on both the taxpayer and the Minister".[1]

[40] Section 248(2) of the ITA is to the same effect. It states that "the tax payable by a taxpayer under any Part of this Act by or under which provision is made for the assessment of tax means the tax payable by the taxpayer as fixed by assessment or reassessment subject to variation on objection or on appeal, if any, in accordance with the provisions of that Part" (emphasis added).

[41] Both ss. 152(8) and 248(2) indicate that until the objection or appeal process is concluded, the amount of tax the minister can compel a taxpayer to pay cannot be known. The assessed amount can change from time to time by virtue of judicial decisions or new

assessments: Terra Nova Properties Ltd. v. M.N.R., [1967] 2 Ex. C.R. 46, [1967] C.T.C. 82 (Exch. Ct.), at p. 51 Ex. C.R. [page547]

[42] The stipulation in s. 158 of the ITA that any unpaid amount assessed is "payable forthwith" upon the mailing of a notice of assessment must be understood within the larger context of the taxpayer's right under the ITA to object to an assessment and to appeal a minister's confirmation of an assessment to the Tax Court of Canada.

[43] Second, Part XV of the ITA places significant restrictions on the minister's ability to collect assessed amounts that are "payable forthwith" where a taxpayer has objected to or appealed those amounts.

[44] Usually, where an amount is payable under the ITA, s. 223(2) authorizes the minister to certify an amount payable that has not been paid "as an amount payable by the debtor". A certificate of an amount payable under ITA, s. 223(2) can be registered in the Federal Court and, when registered, has the same effect as if the certificate were a judgment obtained in the Federal Court against the tax debtor. Sections 223 through 225 then describe the different enforcement steps available to the minister to collect the amount payable: commencing legal proceedings in court; certifying the amount due under s. 223; using statutory garnishment remedies; and seizing the tax debtor's goods and chattels.

[45] However, when a taxpayer files an objection to or appeals an assessment, s. 225.1 places limits on the minister's ability to take steps to collect the assessed amounts. If a taxpayer has served a notice of objection to an assessment, the minister cannot take any of the statutory enforcement steps until 90 days after the minister has sent his notice of confirmation to the taxpayer (s. 225.1(2)). Similarly, if a taxpayer has appealed from an assessment to the Tax Court of Canada, the minister cannot take any of those steps before the day of mailing of a copy of the decision of that court to the taxpayer (s. 225.1(3)).[2]

[46] The rationale behind the limits s. 225.1 places on the minister's ability to collect is that it would be unfair to allow the minister to collect an assessed amount of tax until there is a final determination of the ultimate amount the taxpayer must pay.[3] [page548]

[47] In my view, the Attorney General takes far too narrow an approach to what constitutes an "amount payable" under ITA, s. 223(1), and therefore "personal income tax debt" in BIA, s. 172.1. The Attorney General's submission focuses on only some of the characteristics of an assessed income tax debt -- "payable forthwith" and "valid and binding notwithstanding any error, defect, or omission". It ignores the critical effect of sections 152(8), 225.1 and 248(2) of the ITA that enable a taxpayer to appeal an assessment and limit the collectability of that tax debt by the minister until the courts dispose of the appeal.

[48] When the provisions of the ITA are considered as a whole, the meaning of "amount payable" as used in ITA, s. 223(1) and BIA, s. 172.1(8) must take into account that where a taxpayer has appealed an assessment to the Tax Court of Canada, the actual amount of tax that the minister can compel the taxpayer to pay will not be known until the occurrence of a future event -- i.e., the determination of the taxpayer's appeal from the assessment. This is a hallmark of a contingent claim.

[49] Further, a creditor's inability to enforce a claim bears directly on the creditor's ability to prove its claim under the BIA. In order to be a provable claim within the meaning of BIA, s. 121,

a claim must be one recoverable by legal process: Royal Bank of Canada v. Central Capital Corp. (Re) (1996), 27 O.R. (3d) 494, [1996] O.J. No. 359 (C.A.), at pp. 532-33 O.R. The restraints placed by ITA, s. 225.1 on the enforceability of an assessed amount of tax that is under appeal are strong indicators that a claim based on those amounts would not be provable in a bankruptcy.

[50] Consequently, where amounts of income tax assessed against an individual bankrupt taxpayer remain under appeal at the time of his discharge hearing, the existence of the outstanding appeal entitles the trustee to classify the claim based on the unpaid assessed amounts as a contingent, unprovable one.

C. The jurisprudence

[51] Turning to the jurisprudence, the Attorney General advances two arguments: (i) support for its position can be found in the decision of this court in Norris (Re) (1989), 69 O.R. (2d) 285, [1989] O.J. No. 995 (C.A.); and (ii) the British Columbia and Quebec courts were wrong to conclude in Port Chevrolet (Re) and 2713250 Canada inc. (Re), respectively, that an unpaid assessed amount of tax under appeal is a contingent claim. [page549]

The decision in Norris (Re)

[52] The Attorney General submits that Norris (Re) stands for the principle that in carrying out its duties under the BIA, a trustee cannot ignore what Parliament has legislated with respect to tax debts. Applying that principle to the present case, the Attorney General argues that the trustee must give full recognition to assessed amounts under appeal because under the ITA a taxpayer becomes liable for an unpaid portion of an assessment when the notice of assessment is sent. That liability continues to exist until the assessment is varied or vacated on an objection or appeal.

[53] In my view, the principle in Norris (Re) does not extend as far as the Attorney General submits. That case involved the bankruptcy of an individual against whom an assessment had been issued under the ITA. Critically, unlike in the present case, the bankrupt had not filed a notice of objection to the assessment. The Crown filed a proof of claim in the bankruptcy for the assessed amount and provided the trustee with the notice of assessment. The trustee disallowed the claim. This court held, at p. 287 O.R., that the trustee's request for evidence to support the proof of claim was fully answered by the notice of assessment, and if the trustee in bankruptcy wished to question the validity of an assessment against the bankrupt, it was required to seek its remedy within the ITA by filing a notice of objection.

[54] In the present case, the trustee did not look behind the notice of assessment in order to ascertain the amount of Mr. Schnier's personal income tax debt. Instead, the trustee gave effect to the appeal and enforcement provisions of the ITA. Whether the tax debt was liquidated or contingent for purposes of the BIA depended upon whether the taxpayer had exercised the appeal rights granted by the ITA and, if he had, whether s. 225.1 of the ITA restrained the minister from taking steps to enforce and collect the assessed amount. The trustee took into account that no final determination of Mr. Schnier's appeal had been made under the ITA, with the result that it was unable to value the CRA's claim.

The decisions in Port Chevrolet (Re) and 2713250 Canada inc. (Re)

[55] More relevant to the facts of this case are two decisions dealing with the power of the chair of a meeting of creditors under s. 108 of the BIA to admit or reject a proof of claim for the purpose of voting: Port Chevrolet (Re) and 2713250 Canada inc. (Re). [page550]

[56] In the Port Chevrolet (Re) case, the Canada Customs Revenue Agency ("CCRA") had issued an assessment under the Excise Tax Act, R.S.C. 1985, c. E-15 to Port Chevrolet for about $16.4 million. The company filed a notice of intention to make a proposal under the BIA. The company also filed a notice of objection to the assessment. The CCRA filed a proof of claim in the amount of about $15.8 million the day before the meeting of creditors to vote on the company's proposal. The trustee disallowed CCRA's claim and valued it at nil, taking the view that it was unproven because it was based on an unresolved appeal and notice of objection. Relying on the trustee's disallowance, the chair of the creditors' meeting concluded that the CCRA claim was contingent and valued it at nil for voting purposes.

[57] The CCRA appealed the trustee's disallowance of its claim and the chair's decision that it had no right to vote at the meeting. The chambers judge dismissed the appeal on two grounds. First, the CCRA had failed to file a proof of claim in proper form: at para. 25. Second, the court rejected the CCRA's argument that provisions in the Excise Tax Act analogous to ss. 152(8) and 158 of the ITA created a valid and binding debt due from the moment of assessment regardless of the pending objection and appeal process: at paras. 35-36. The court stated, at para. 43:

> [I]f CCRA wishes to participate in concurrent proceedings under the Bankruptcy and Insolvency Act, then it is bound to comply with the Bankruptcy and Insolvency Act process with respect to proving its claim, and that compliance includes recognition of the trustee's powers to determine a claim is contingent and value it accordingly. I do not read Re Norris as precluding a trustee from exercising his discretion under s. 135(1.1).

[58] The British Columbia Court of Appeal affirmed the decision, but only in respect of the finding that the CCRA had failed to file a proof of claim in proper form. The BCCA specifically declined to consider the trustee's disallowance of the CCRA's contingent claim.

[59] A similar issue arose in a Quebec case involving a proposal made by 2713250 Canada Inc. under the BIA. The Agence du revenue du Québec ("ARQ") had issued two notices of assessment to the debtor company for which the company had filed notices of objection. The ARQ filed proofs of claim in the proposal proceedings based upon the full amount of the assessments. At two meetings of creditors, the proposal trustee held that the ARQ's claims were contingent and impossible to value because of the pending appeal of the notices of assessment. [page551] Therefore, the ARQ was ineligible to vote. The ARQ appealed the trustee's decisions.

[60] Gascon J., as he then was, dismissed the appeal, applying the reasoning of the chambers judge in the Port Chevrolet (Re) case. He held that in exercising the power conferred on it by BIA, s. 108(1), the trustee could conclude that the ARQ's claims were in fact contingent, unliquidated and not provable claims, due to the impossibility of valuing them with any certainty: at para. 86. Gascon J. then considered, and rejected, the ARQ's argument about the validity and binding nature of its notices of assessment, at paras. 88 through 94:

> Contrary to what the ARQ argues, the Court believes that in exercising the power ascribed to it by section 108(1), the Trustee was not legally bound to consider as valid, regardless of the situation, the notices of assessment on which the disputed proofs of claims are based.
>
> On the one hand, if the relevant tax laws establish a presumption of validity of those notices of assessment, that presumption is not irrebuttable. The objection process such tax laws authorize surely demonstrates this.
>
> On the other hand, the presumptions of validity established by tax laws are not incompatible with the exercise of the jurisdiction which the BIA confers on the Trustee pursuant to sections 108, 121 or 135 of the BIA.
>
> As the Court of Appeal for British Columbia points out in its analysis of the problem in Port Chevrolet, there are two possible solutions under such circumstances.
>
> The first is that in terms of a proof of claim filed under the BIA, one must give, without reservation, full faith and credit to any notice of assessment by the tax authorities, regardless whether it may eventually be set aside.
>
> The second is that we can reconcile the BIA and tax laws by drawing a distinction between, on the one hand, business judgment and a trustee's practice in exercising its powers under the BIA and, on the other hand, the "rebuttable" presumptions of validity of tax laws which subsist notwithstanding the prescribed objection and appeal processes.
> For its part, the Court prefers the second solution, which is much more respectful of the objectives of the BIA.

(Translation from French)

[61] Although the Port Chevrolet (Re) and 2713250 Canada Inc. (Re) cases both involved the exercise by trustees of their discretion in the context of admitting or rejecting proofs of claim for the purposes of voting under BIA, s. 108(1), in my view the reasoning in Port Chevrolet (Re), as adopted by 2713250 Canada inc. (Re), applies equally to the exercise of the trustee's general power to determine whether a contingent claim is a provable claim under ss. 121 and 135 of the BIA. Where a bankrupt taxpayer has appealed assessed amounts of income tax, it is open to a trustee to characterize a CRA proof of claim based on those [page552] assessments as a contingent claim. If the claim cannot be valued with any certainty prior to the disposition of the appeal, the trustee may treat the contingent claim as not provable in the bankruptcy.

[62] Such a result gives full recognition to the provisions of the ITA discussed earlier dealing with the calculation and enforcement of assessed amounts of income tax, while treating a proof of claim based on an appealed assessment in a manner harmonious with the general scheme of the BIA concerning creditors' proofs of claim.

[63] Such an interpretation is also consistent with the language of s. 172.1(1) of the BIA, which provides that the special discharge rules for tax-driven personal bankruptcies apply "in the case of a bankrupt who has $200,000 or more of personal income tax debt and whose personal income tax debt represents 75% or more of the bankrupt's total unsecured proven claims" (emphasis added). The use of the word "represents" signifies that in order for "personal income tax debt" to be capable of representing 75 per cent of a bankrupt's unsecured "proven claims", the "personal income tax debt" must possess the characteristics of a provable claim in

bankruptcy. Put another way, to qualify as "personal income tax debt" within the meaning of s. 172.1(1), the tax debt must be a proven claim.

[64] To hold otherwise would give unfair, preferential treatment to CRA proofs of claim based on assessed income tax amounts that remain under appeal at the time of a discharge hearing. If the full amount of the assessed amount under appeal was recognized as a claim provable in the bankruptcy, and the taxpayer's appeal of the assessment was later allowed and the assessed amount reduced or eliminated, the CRA would have obtained an unjustified advantage over other creditors in the bankruptcy proceeding.

D. Potential abuse of the bankruptcy process

[65] Against that conclusion, the Attorney General argues that to treat CRA claims for unpaid assessed income tax under appeal as contingent ones that may not be provable would render meaningless s. 172.1 of the BIA. A taxpayer who was subject to significant income tax assessments could abuse the bankruptcy process by appealing his assessment, then make an assignment in bankruptcy and fail to expedite the hearing of his tax appeal. That would allow a bankrupt to avoid the special discharge rules created by s. 172.1 for tax-driven bankruptcies.

[66] In my view, the motion judge correctly addressed this argument when he held that "an adjournment could have been [page553] sought before the [registrar] so the appeal could be heard and no attempt was made in this case". Indeed, had the CRA sought a brief adjournment of Mr. Schnier's discharge hearing, no dispute could have arisen about the applicability of s. 172.1 to his bankruptcy, as the following chronology of events discloses.

[67] Section 225.1(5) of the ITA states that where a taxpayer who has appealed to the Tax Court of Canada has agreed to delay his appeal until the court has decided related test cases, then the minister may take actions to enforce the assessments against the taxpayer at any time after the minister gives written notice to the taxpayer that the decision of the Tax Court of Canada in the test case has been mailed to the minister.

[68] In February 2012, Mr. Schnier had filed with the Tax Court of Canada his agreement to be bound in the lead test cases before that court concerning the deductibility of expenses relating to the yacht tax shelters. The Tax Court of Canada confirmed that it would hold his appeal in abeyance pending the resolution of the three lead test cases. The lead cases concerning the yacht tax shelters were dismissed on January 7, 2014, and an appeal from that dismissal to the Federal Court of Appeal was withdrawn on March 19, 2014. Both those events took place before Mr. Schnier's bankruptcy hearing.

[69] However, the Tax Court of Canada did not formally dismiss Mr. Schnier's appeal from the yacht tax shelter assessments until August 18, 2014, slightly more than a month after his discharge hearing was held. The record does not explain when the Tax Court of Canada mailed the minister the decision dismissing the lead test appeals concerning the yacht tax shelters or why the minister did not send a written notice of the decision to Mr. Schnier prior to his discharge hearing. From the transcript of the discharge hearing, it is apparent that the parties were aware the test cases had been resolved in favour of the CRA: appeal book, p. 56. Why, given those circumstances, the CRA did not ask for a short adjournment of the discharge hearing pending formal notice to Mr. Schnier of the dismissal of the lead test appeals pursuant to ITA, s. 225.1(5) was not explained in the record before us.

E. Whether the trustee disallowed any part of the claim

[70] Finally, in her factum, the Attorney General argued that the trustee had failed to determine whether or not the CRA's claim was provable. I disagree.

[71] Although the appeal record did not contain a notice of disallowance issued by the trustee under BIA, s. 135(3) in respect of [page554] the claim, appellant's counsel candidly conceded that there was no evidence before the court about what, if anything, the trustee did under s. 135.

[72] In any event, the evidence showed that the CRA was aware well before the discharge hearing that the trustee had disallowed that part of its claim covering the assessed amounts under appeal. The trustee's report under s. 170(1) on the bankrupt's application for discharge was dated February 4, 2014, some five months prior to the discharge hearing, and was signed by the inspectors, including one of the inspectors who was an employee of the CRA. The report clearly stated that the trustee was unable to value most of the CRA's claim and had not admitted the portion concerning the assessed amounts under appeal as it was contingent. The trustee's July 9, 2014 claims register also recorded that $4.385 million of the CRA claim had been classified as contingent and had not been admitted for dividend. Accordingly, the evidence before the registrar at the time of the discharge hearing was that the trustee had determined that only $71,170 of the CRA claim was provable in the bankruptcy.

F. Conclusion

[73] For the reasons set out above, I conclude that both the motion judge and the registrar were correct in concluding that until the Tax Court of Canada disposed of Mr. Schnier's appeals of the CRA's assessments, the CRA's claim in the bankruptcy for the assessed amount under appeal was a contingent one which the trustee could refuse to admit as a proven claim. Consequently, the motion judge and the registrar correctly concluded that s. 172.1 of the BIA did not apply to Mr. Schnier's discharge hearing.

VI. Disposition

[74] I would dismiss the appeal. The parties agreed that the successful party would be entitled to costs of the appeal on a partial indemnity basis in the amount of $15,000. I would therefore order the Attorney General of Canada to pay Mr. Schnier costs of $15,000, inclusive of HST and disbursements.

Appeal dismissed.

[page555]

Notes

1 Moreover, the case law interpreting s. 152(8) treats the section's purpose as a modest one, operating as a curative provision ensuring the validity of an administratively issued assessment despite any errors, defects or omissions: Regina Shoppers Mall Ltd. v. Canada, [1991] F.C.J. No. 52, [1991] 1 C.T.C. 297 (C.A.), at p. 301 C.T.C.; Leung v. Canada, [1993] F.C.J. No. 942, [1993] 2 C.T.C. 284 (T.D.), at p. 302 C.T.C.

2 Although ITA, s. 225.1 provides for certain exceptions to these bars to collection, none apply to the facts of the present case.

3 If reasonable grounds exist to believe that the collection of an assessed amount would be jeopardized by a delay in collection, ITA, s. 225.2 authorizes the minister to apply ex parte to the court for an order allowing him to take enforcement steps.

End of Document

TAB 24

COURT OF APPEAL

CANADA
PROVINCE OF QUEBEC
REGISTRY OF MONTREAL

No.: 500-09-030055-222
(500-11-045951-148)

DATE: March 20, 2023

CORAM: THE HONOURABLE MARK SCHRAGER, J.A.
GUY COURNOYER, J.A.
SOPHIE LAVALLÉE, J.A.

IN THE MATTER OF THE BANKRUPTCY OF:
SOCIÉTÉ DE VÉLO EN LIBRE SERVICE/PUBLIC BIKE SYSTEM COMPANY
BANKRUPT – Debtor
and
ARTHUR BLUMER & ASSOCIÉS INC., in continuance of suit for Litwin Boyadjian Inc.
APPELLANT – Trustee
v.

VILLE DE MONTRÉAL
RESPONDENT – Creditor/Petitioner

JUDGMENT

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[1] On appeal from a judgment rendered on May 5, 2022 by the Superior Court, Commercial Division, District of Montreal (the Honourable Justice Martin Castonguay), dismissing in part the Appellant's disallowance of the Respondent's proof of claim in the bankruptcy of Société de vélo en libre-service/Public Bike System Company.

[2] For the reasons of Schrager, J.A., with which Cournoyer and Lavallée, JJ.A. agree, **THE COURT:**

[3] **DECLARES** that the Appellant has an appeal as of right, such that leave is not required, and **DISMISSES** the Appellant's *De Bene Esse* Application for Leave to Appeal a Judgment Rendered in the Course of Bankruptcy Proceedings, without costs;

[4] **ALLOWS** the appeal;

[5] **SETS ASIDE** the judgment of the Superior Court, Commercial Division, District of Montreal (the Honourable Justice Martin Castonguay) rendered on May 5, 2022;

[6] **DISMISSES** the Respondent's appeal from the Trustee's Notice of Disallowance of proof of claim dated December 15, 2020;

[7] **TAKES COGNIZANCE** of the withdrawal of the Notice of Disallowance dated December 15, 2020, issued by the Appellant to the Respondent, solely with respect to the disallowance of the portion of the re-amended Proof of Claim related to the suretyship agreement dated June 1, 2011, entered into between National Bank of Canada (the "Bank") and the Respondent, the payment by the Respondent to the Bank made on April 30, 2014, in an amount of $6,489,081.12, the *Modalités relatives au paiement des sommes dues par Société de vélo en libre-service à Banque Nationale du Canada*, being Schedule "A" to the re-amended Proof of Claim, and the payment by the Respondent to the Bank made on June 10, 2014, in an amount of $1,702,600.00;

[8] **THE WHOLE** with costs against the Respondent in first instance and in appeal.

MARK SCHRAGER, J.A.

GUY COURNOYER, J.A.

SOPHIE LAVALLÉE, J.A.

Mtre Alain Tardif
Mtre Gabriel Faure
Mtre Marc-Étienne Boucher
MCCARTHY TÉTRAULT
For the Appellant

Mtre Se-Line Duong
Mtre Eleni Yiannakis
Mtre François Goyer
IMK
For the Respondent

Date of hearing: February 9, 2023

REASONS OF SCHRAGER, J.A.

[9] This is an appeal from the judgment rendered on May 5, 2022 by the Superior Court, Commercial Division, District of Montreal (the Honourable Martin Castonguay).[1]

[10] The judgment sets aside, in part, the disallowance by the Appellant-Trustee[2] of the Respondent's proof of claim in the bankruptcy of Public Bike System Company ("**Bixi**") and declares that the Respondent[3] is an unsecured creditor for an amount of $31,746,757 ranking *pari passu* with the other unsecured creditors.

[11] For the reasons which follow, I propose that the Court allow the appeal, overturn the judgment under appeal and dismiss the Respondent's appeal from the Trustee's notice of disallowance of its proof of claim.

I. FACTS

[12] The partial disallowance of the Respondent's claim pertains to the following sums of money:

- $8,191,681.12 due by Bixi to the Respondent and arising from payments by the Respondent to Bixi's banker pursuant to a guarantee signed by the Respondent;

- $31,746,575 due by Bixi to the Respondent for a direct loan that was declared null by the Court in a previous judgment.[4]

[13] The text of the disallowance reads in part as follows:

> 2. With respect to Ville de Montreal's entire claim in the amount of $39,938,256.12:
>
> • Ville de Montreal was not dealing at arm's length with the debtor when it entered into the various transactions at the basis of its claim, as held by the Court of Appeal at paragraphs 67 and following of its judgement in *Ville de Montreal c. Litwin Boyadjian inc*. (*Syndic de Société de vélo en libre-service*), 2019 QCCA 794. In the Trustee's opinion, these transactions

1 *Syndic de Société de vélo en libre service*, 2022 QCCS 1638 [Judgment under appeal].
2 Herein the "Trustee" or the "Appellant".
3 Herein the "Respondent" or the "City".
4 *Ville de Montréal v. Litwin Boyadjian inc. (Syndic de Société de vélo en libre-service)*, 2019 QCCA 794, leave to appeal to the Supreme Court of Canada refused 2020 CanLII 13146 (SCC) [*2019 Judgment*].

> cannot be deemed "proper" within the meaning of section 137(1) of the Act, as they were entered into in violation of the Municipal Aid Act, a legislation of public order intended to protect taxpayers against municipal mismanagement of public funds. The City's claim must thus be postponed pursuant to section 137(1) of the Act.
>
> • Alternatively, Ville de Montréal's claim must be characterized as an equity claim and postponed accordingly pursuant to section 140.1 of the Act. Pursuant to the recharacterization doctrine, the Trustee must consider the manner in which the underlying transactions were implemented and the economic reality of the surrounding circumstances. The record shows *inter alia* that Ville de Montréal intervened to regularize the Bankrupt's financial situation at a time when the latter could not find other sources of financing in order to uphold the Debtor's bike-sharing services for the benefit of its citizens. Moreover, the Convention de prêt dated May 27, 2011 was mostly used to reimburse the Bankrupt's starting capital (initially itself lent by Société en commandite Stationnement de Montréal). In short, the transactions at the basis of Ville de Montréal's claim must be recharacterized as capital contributions.

[14] It is common ground that the Respondent's claim, if not postponed, would seriously dilute the distribution to the unsecured creditors of Bixi from the approximate amount of $21,000,000 held by the Trustee for such purpose. If the claim is postponed, the Respondent will not receive any dividend.

[15] The Court's *2019 Judgment* referred to above[5] declared that the loan advanced by the Respondent to Bixi and the hypothec granted to secure it were null as they offended a provision of public order prohibiting municipalities from offering financial assistance to commercial establishments.[6] However, the judgment went on to declare that the Respondent was nevertheless a creditor of Bixi (in an amount of $31,746,575) since the nullity of the loan agreement gave rise to the obligation of restitution between the parties, such that Bixi should return the loan proceeds received from the Respondent. However, since the bankruptcy of Bixi made it impossible for Bixi to pay the monies to the Respondent, the Court modified the manner of making restitution and recognized that the Respondent could file a proof of claim in the bankruptcy.

[16] As set forth above, the Trustee disallowed the Respondent's proof of claim and the claims were postponed. The Respondent's appeal from the Trustee's disallowance was allowed in part by the Superior Court. The judge overruled the Trustee's postponement regarding the portion of $31,746,575 only. He accepted the Respondent's argument that the *2019 Judgment* created a new "legal reality" between the parties such that the source

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5 *2019 Judgment*, *supra*, note 4.

6 *Municipal Aid Prohibition Act*, CQLR, c. I-15.

of the Respondent's claim was not the loan contract that had been declared null but rather the obligation to make restitution. Accordingly, s. 137 of the *Bankruptcy and Insolvency Act*[7] ("***BIA***") invoked by the Trustee to justify the postponement did not apply. Such provision allows for the postponement of claims arising from contracts that are entered into between a bankrupt and non-arm's-length parties and are not proper. The judge added that the Respondent did deal at arm's length with Bixi since they were not related according to the definitions found in ss. 4(2) and 4(3) *BIA*. The judge also made short shrift of the Trustee's reliance on s. 140.1 *BIA* to contend that the claim represented equity and not debt. The judge stated that the proof in the record indicates the Respondent's intention to be reimbursed the advances made to Bixi, so that the money advanced was a loan and not a contribution to capital.

[17] As stated above, I believe the appeal should be allowed as the judgment is tainted by both errors of law and errors of mixed fact and law.

II. ISSUES

[18] The parties' respective positions give rise to four issues for resolution on appeal:

1.- Does the Appellant have an appeal as of right or does it require leave and, if so, should leave be granted pursuant to the *De Bene Esse* application for such leave referred to this panel?

2.- Did the judge err in concluding that the Court already decided in the *2019 Judgment* that the Respondent's claim as an unsecured creditor should be allowed by the Trustee?

3.- Did the judge err in the interpretation and application of s. 137 *BIA*?

4.- Did the judge err in concluding that the Trustee's determination that the Respondent's claim was an "equity claim" was unreasonable?

III. ANALYSIS

1.- Does the Appellant have an appeal as of right or does it require leave and, if so, should leave be granted pursuant to the *De Bene Esse* application for such leave referred to this panel?

[19] The Appellant's notice of appeal relies upon paragraph (a) – the point at issue involves future rights – and paragraph (c) – the property involved in the appeal exceeds in value $10,000 – of s. 193 *BIA*.

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[7] R.S.C. (1985), c. B-3.

[20] The Appellant has also applied for leave to appeal under s. 193 (e) *BIA* in the event the Court rules that it has no appeal as of right. That application was referred to the Court by one of our colleagues.[8]

[21] Given that the question of the postponement of the Respondent's proof of claim would mean that the Respondent would not share in any dividend in the Bixi bankruptcy, the Appellant contends that the value of the property involved in the appeal exceeds $10,000.[9] I believe this to be the case. Moreover, there is abundant case law confirming that where the amount at issue in a proof of claim exceeds $10,000, a right of appeal under s. 193 (c) *BIA* exists. Ultimately, if the issue is the loss or gain resulting from the disallowance or acceptance of a proof of claim for more than $10,000, s. 193 (c) *BIA* permits an appeal.[10]

[22] However, the Respondent argues, based primarily on the decision of Brown, J.A., sitting as chamber's judge, in *2403177 Ontario Inc. v. Bending Lake Iron Group Limited*,[11] that s. 193 (c) *BIA* should be read restrictively and not apply to "(i) orders that are procedural in nature; (ii) orders that do not bring into play the value of the debtor's property; or (iii) orders that do not result in a loss".[12]

[23] To put the decision in context, *Bending Lake* involved an appeal from a judgment approving a sale agreement and ordering the vesting of the debtor's property. The value of the property was not in issue. Rather, the grounds of appeal were "process-related", regarding such things as disclosure of information about the sale agreement to the debtor by the receiver, the negotiation process for the sale and the adequacy of notice given to Aboriginal communities.[13]

[24] In *Hillmount Capital inc. v. Pizale*,[14] Brown, J.A. revisited s. 193 (c) *BIA* and agreed with the Saskatchewan Court of Appeal in *MNP Ltd. v Wilkes*[15] that merely because the question raised in appeal is procedural, this does not mean there is not property involved that exceeds $10,000. Thus, the Court should scrutinize the grounds of appeal to examine the effect of the order sought.[16]

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8 *Syndic de Société de vélo en libre-service*, 2022 QCCA 853 (Cournoyer, J.A.).

9 Property is defined in s. 2 *BIA* as including "money".

10 See, for example, *Trimor Mortgage Investment Corporation v. Fox*, 2015 ABCA 44, paras. 7-10; *Roman Catholic Episcopal Corporation of St. George's v. John Doe - 49 - GBS*, 2007 NLCA 17, paras. 22-27; *Temple Consulting Group Ltd. v. Abakhan & Associates Inc*., 2011 BCCA 540, paras. 5-8; *EnerNorth Industries Inc. (Re)*, 2009 ONCA 536, para. 34.

11 *2403177 Ontario Inc. v. Bending Lake Iron Group Limited*, 2016 ONCA 225 [*Bending Lake*].

12 *Bending Lake*, *supra*, note 11, para. 53; but, see also *Orpen v. Roberts*, [1925] S.C.R. 364, p. 367: Pecuniary loss is the determinant of whether a monetary threshold has been crossed.

13 *Bending Lake*, *supra*, note 11, para. 58.

14 *Hillmount Capital Inc. v. Pizale*, 2021 ONCA 364 [*Hillmount Capital*].

15 *MNP Ltd. v Wilkes*, 2020 SKCA 66.

16 *Hillmount Capital*, *supra*, note 14, paras. 41-42.

[25] In the present case, the value of the Respondent's claim is inextricably the issue as it is common ground that if it is postponed, it will be worthless in a distribution and will result in a loss for the Respondent exceeding $30,000,000. Moreover, if not postponed, the claim will cause considerable dilution, exceeding in the aggregate $10,000, of the payment to all other creditors. This appeal clearly involves a potential loss either to the Respondent or to the mass of creditors exceeding the threshold amount; it is not restricted to procedural issues.

[26] Accordingly, I would conclude that the Appellant has a right of appeal under s. 193 (c) *BIA*.

[27] If I doubted the existence of an appeal as of right, I would not hesitate to grant leave as requested by the Appellant because the criteria for the granting of such leave are easily satisfied.[17]

[28] The appeal is, at the very least, *prima facie* meritorious, its resolution is important for this bankruptcy estate, and the issues raised bear on the law in the area. No undue delay in the administration of the bankrupt estate is caused at this point in time by the appeal.

[29] However, I propose to dismiss the application for leave, without costs, as being unnecessary given my opinion that there is a right of appeal under s. 193 (c) *BIA*.

2.- Did the judge err in concluding that the Court already decided in the *2019 Judgment* that the Respondent's claim as an unsecured creditor should be allowed by the Trustee?

[30] The conclusions of the *2019 Judgment* state simply:

> [76] **ACCUEILLE** partiellement l'appel, avec les frais de justice, à seule fin d'ajouter une conclusion déclaratoire :
>
> > **DÉCLARE** que la Ville est créancière pour le solde dû à la date de la prise en paiement, soit 31 746 575 $, et peut présenter une réclamation au syndic de faillite;

Though the doctrine of *res judicata* can extend beyond the conclusions (in French "*dispositif*") of a judgment to the reasons, the latter must be intrinsically tied to such

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[17] *CHU de Québec - Université Laval v. Busrel inc*., 2022 QCCA 562.

conclusions.[18] In principle, it is the conclusions which are operative.[19]

[31] As stated above, the Court examined the validity of the loan made by the Respondent to Bixi and the security, in light of the legal prohibition against such financial assistance.[20] The Court found that the nullity gives rise to the obligation of restitution pursuant to art. 1422 *C.C.Q.* and then added the following:

> [62] La faillite subséquente de Bixi l'empêche de remettre le prêt obtenu. Par ailleurs, ordonner à la Ville seule de restituer les prestations créerait un déséquilibre et avantage injustifié pour Bixi. La solution adéquate est de modifier les modalités de la restitution en reconnaissant que la Ville est créancière de Bixi pour le solde du prêt et qu'elle peut présenter une réclamation dans la faillite[27], en application du deuxième alinéa de l'article 1699 *C.c.Q.* Cette créance est sujette aux règles de droit régissant la faillite (art. 69.3 LFI). Sa créance sera traitée *pari passu* avec les autres créanciers de la faillite. Le prêt et l'hypothèque sont nuls, mais l'obligation pour Bixi de restituer l'argent reçu existe en application du principe de restitution des prestations.
>
> [63] À la lecture du jugement, il est impossible de savoir si le juge estime que Bixi n'a pas à rembourser le prêt ou s'il a tenu pour acquis que la Ville possède une créance et va déposer une réclamation dans la faillite. Il convient d'ajouter une conclusion à cet effet.
>
> (Emphasis added)

[32] The Court's language is permissive – i.e. the City "peut présenter une réclamation dans la faillite" and any such proof of claim will be subject to the legal rules governing the bankruptcy.

[33] No such proof of claim had been filed at the time of the *2019 Judgment*. As such, the Court cannot be taken to have ruled on the validity or propriety of such claim. Nevertheless, the Respondent submits that the use of the term "*pari passu*" in paragraph 62 refers to how such claim should be treated or collocated in the bankruptcy. The judge evidently agreed:

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18 *Ellard v. Millar*, 1929 CanLII 55 (SCC), [1930] S.C.R. 319, 326, Rinfret, J.; *Contrôle technique appliqué ltée v. Québec (Procureur général)*, 1994 CanLII 5595 (C.A.), [1994] R.J.Q. 939, pp. 943 and 944, cited in *Jean-Paul Beaudry ltée v. 4013964 Canada inc*., 2013 QCCA 792, para. 37 – see also para. 39 citing Jean-Claude Royer and Sophie Lavallée, *La preuve civile*, 4th ed., Cowansville, Les Éditions Yvon Blais inc., 2008, pp. 690-691: "L'autorité de la chose jugée peut également s'étendre à des motifs étroitement reliés au dispositif du jugement".

19 *Compagnie d'assurances générales Co-Operators v. Coop fédérée*, 2019 QCCA 1678, paras. 112-113; *Syndic de Mekenthiram*, 2022 QCCA 197, para. 3.

20 *2019 Judgment*, *supra*, note 4, para. 8.

> [35] De fait, le Syndic, en ajournant la preuve de réclamation de la créance de la Ville telle qu'établi par la Cour d'appel, fait comme si cet arrêt n'existait tout simplement pas ou encore que la décision de la Cour supérieure maintenue par la Cour d'appel, n'avait aucun impact sur le pouvoir par le Syndic, d'analyser le bien-fondé d'une preuve de réclamation sous le prisme de l'article 137(1) L.F.I.
>
> [36] C'est l'existence même de l'arrêt et en particulier son paragraphe 62 lequel doit être lu en conjonction avec tous ceux de la section « La restitution par Bixi » qui fait en sorte que la position du Syndic est non seulement déraisonnable, mais frôle la témérité.

[34] The Respondent and the judge read into the *2019 Judgment* what is not there. As stated, the Court was not examining a proof of claim but merely the City's right to file a proof of claim and thereby become a creditor in the bankruptcy.[21] In the brief the Respondent had filed in that case, it had indeed sought to have its claim (as opposed to its right to file a proof of claim) recognized, but that is not what the Court did.

[35] Counsel for the Respondent points to the second paragraph of Article 1699 *C.C.Q.*:

1699. (…)	**1699.** […]
The court may, exceptionally, refuse restitution where it would have the effect of according an undue advantage to one party, whether the debtor or the creditor, unless it considers it sufficient, in that case, to modify the scope or modalities of the restitution instead.	Le tribunal peut, exceptionnellement, refuser la restitution lorsqu'elle aurait pour effet d'accorder à l'une des parties, débiteur ou créancier, un avantage indu, à moins qu'il ne juge suffisant, dans ce cas, de modifier plutôt l'étendue ou les modalités de la restitution.

Thus, the Respondent argues that it was open to the Court in the *2019 Judgment* to subordinate the City's claim if it obtained an undue advantage. Given that the Court did not do this, counsel reasons that the Court did not believe the City obtained an undue advantage, such that the Trustee is bound to consider the 2011 transaction a proper one and not invoke s. 137 to subordinate the Respondent's claim. Again, counsel reads into the *2019 Judgment* what is not there. There is no indication that this was considered. It is not for this panel to add to what the Court wrote in paragraph 62 of the *2019 Judgment* quoted above.

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[21] Section 124 *BIA*.

[36] Nowhere did the Court put aside or even refer to the Trustee's duty "to examine every proof of claim (…) and the grounds therefor" and to make a determination, as required by s. 135 (1) *BIA*. This duty is a fundamental obligation of a bankruptcy trustee.[22]

[37] The expression "*pari passu*" in paragraph 62 of the *2019 Judgment* refers to the right of the Respondent, like other creditors, to file a proof of claim, not to its eventual treatment or collocation by the Trustee. The Court did not say that the claim would be paid rateably (in French "*au prorata*"), which is the general rule, set out in s. 141 *BIA*, for dealing with claims; the Court merely stated that the claim would be treated as all the other claims. This includes the examination by the Trustee pursuant to s. 135.

[38] The reference in paragraph 75 of the *2019 Judgment* to such proof of claim as "*chirographaire*" or ordinary or unsecured, in the context of the *2019 Judgment*, clearly refers to the fact that the loan and the accessory hypothec were null but that the legal institution of restitution would give rise to the City's right to claim the monies advanced to Bixi, albeit not as a secured creditor.

[39] Moreover, the postponement of the Respondent's claim pursuant to the Trustee's notice of disallowance does not *per se* contradict that the Respondent is an unsecured ("*chirographaire*") creditor. The disallowance maintains such qualification but postpones the claim, or in the wording of ss. 137 and 140.1 *BIA*, the Respondent is not entitled to receive a dividend in the bankruptcy until the other unsecured creditors are fully paid.

[40] The Respondent points to comments from one member of the panel and exchanges with counsel to bolster its position that the Court decided in the *2019 Judgment* that the proof of claim was valid. However, comments from the panel are not binding and do not form any part of a judgment.[23]

[41] I believe that the foregoing analysis indicates that the conclusions of the *2019 Judgment*, taken alone or in conjunction with the reasons, disclose a decision providing for the Respondent's right to file a claim as an unsecured creditor in the bankruptcy of Bixi in the amount stated. Neither the conclusions nor the reasons address the eventual treatment of that claim by the Trustee in the exercise of its duties under s. 137 *BIA*. In deciding otherwise, the judge committed a reviewable error, which merits intervention by the Court.

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22 *Sellathamby (Re)*, 2020 BCSC 1567, para. 35; *Royal Bank of Canada v. Insley*, 2010 SKQB 17, paras. 23-24; *Huphman (Re)*, 2019 NSSC 280, para. 18; *Constructions d'Argenson inc. (Proposition de)*, 2000 CanLII 19269 (QC CS), para. 15.

23 *M.R. v. Hall*, 2021 QCCA 826, para. 26.

3.- Did the judge err in the interpretation and application of s. 137 *BIA*?

[42] The judge concluded that the Trustee was wrong to postpone the Respondent's claim pursuant to s. 137(1) *BIA*. It provides as follows:

137 (1) A creditor who, at any time before the bankruptcy of a debtor, entered into a transaction with the debtor and who was not at arm's length with the debtor at that time is not entitled to claim a dividend in respect of a claim arising out of that transaction until all claims of the other creditors have been satisfied, unless the transaction was in the opinion of the trustee or of the court a proper transaction.	**137 (1)** Le créancier qui, avant la faillite du débiteur, a conclu une transaction avec celui-ci alors qu'il existait un lien de dépendance entre eux n'a pas droit de réclamer un dividende relativement à une réclamation née de cette transaction jusqu'à ce que toutes les réclamations des autres créanciers aient été satisfaites, sauf si la transaction était, de l'avis du syndic ou du tribunal, une transaction régulière.

[43] The judge held that s. 137 *BIA* did not apply because the Respondent and Bixi did deal at arm's length. He reasoned that since they were not related within the meaning of ss. 4 (2) and 4 (3) *BIA*, then in virtue of s. 4 (5) they could not be deemed not to deal at arm's length. This is an error of law as the judge failed to consider s. 4 (4) *BIA* which provides as follows:

4 (4) It is a question of fact whether persons not related to one another were at a particular time dealing with each other at arm's length.	**4 (4)** La question de savoir si des personnes non liées entre elles n'avaient pas de lien de dépendance, à tel ou tel moment, est une question de fait.

[44] Thus, even though the Respondent and Bixi might not have been related parties within the definition of s. 4 *BIA* (and I express no opinion on such finding), the judge should have pursued his analysis to see if the facts indicated that they were or were not arm's length parties. The factual matrix is compelling: (i) Bixi was executing the Respondent's bicycle sharing project on its behalf as the Court observed in the *2019 Judgment*;[24] (ii) Bixi's project was conceived by Mr. André Lavallée, an elected official of the Respondent; (iii) the Respondent's treasurer was also a member of the board of directors of Bixi from 2001 to 2013 and was extensively involved in the financing referred to above, as the Court observed in the *2019 Judgment*;[25] and (iv) the Respondent's consolidated financial statements included those of Bixi together with other entities under the Respondent's control.

[45] Moreover, the judge did not consider the scope of the agreement entered into between the Respondent and Bixi in 2011, whereby Bixi effectively gave the Respondent

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[24] 2019 Judgment, *supra*, note 4, paras. 4-5.

[25] 2019 Judgment, *supra*, note 4, para. 40 (referring to para. 110 of the trial judgment on appeal to the Court in that case).

de jure control over it. Pursuant to such agreement, *inter alia*: (i) the members and the chairman of Bixi's board of directors and its managing director were appointed on the recommendation of the Respondent; (ii) Bixi was obliged to submit to the Respondent, for approval, its budgets and three-year plans on such dates and in such form and substance as the Respondent indicated; (iii) Bixi was obliged to inform the Respondent of any major change to its approved budget; (iv) Bixi was obliged to remit to the Respondent yearly audited financial statements, quarterly interim financial statements, and quarterly detailed reports of its operations and orientations ("*reddition de compte complète […] de ses activités et de ses orientations*"); (v) Bixi granted the Respondent unfettered access to its books, records and premises; (vi) Bixi undertook to abide by the rules governing the awarding of contracts under the *Cities and Towns Act*; and (vii) Bixi undertook not to contract debt financing, modify its corporate structure, merge with any entity, modify its letters patent or seek its dissolution without the prior approval of the Respondent. These elements are not addressed in the judgment.

[46] In view of the above, it is not surprising that in the *2019 Judgment*, the Court, in applying s. 95 (1) (b) *BIA* to the transaction between the Respondent and Bixi, underlines the following passage of the provision:[26]

> (…) a creditor who is not dealing at arm's length with the insolvent person (…)

[47] Lastly, during argument before the judge, counsel for the Respondent conceded that his client was related to Bixi: "*C'est pas contesté que la Ville est une personne liée à Bixi, c'était notre conclusion à l'époque, ça été la conclusion de la Cour d'appel, c'est pas un fait qui est contesté*".

[48] Accordingly, in deciding that s. 137 (1) *BIA* was not applicable, the judge erred both in law and in fact.

[49] However, the Respondent asserts (and the judge agreed) that the effect of the *2019 Judgment* providing for restitution creates a new "legal reality" between the parties – i.e. the restitution obligation to return the funds received is the source of the obligation, such that the propriety of the transaction between the Respondent and Bixi in 2011 was not to be considered in examining the Respondent's proof of claim.

[50] I believe this argument is wrong in law for the reasons that follow.

[51] That the concept of restitution allowed the Respondent to file a proof of claim regarding proceeds of a loan declared null does not mean that logically or legally the Appellant in the performance of its trustee's duty to examine that claim "and the grounds therefor",[27] should not look beyond the obligation of the bankrupt to make restitution and

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[26] 2019 Judgment, *supra*, note 4, para. 67.

[27] Section 135 (1) *BIA*.

consider the circumstances giving rise to the claim. Such consideration would include the elements giving rise to the nullity of the contract as examined by the Court in the *2019 Judgment*. That judgment has the effect of setting aside the obligation generated by the contract of loan but does not somehow erase the historical fact of that loan transaction so that a trustee should close its eyes to it, pretending that it never existed. As a majority of the Supreme Court observed recently in dealing with a municipal contract declared a nullity:

> (…) it will then be deemed never to have existed (arts. 1416 and 1422 *C.C.Q.*; Cumyn, at No. 224; Lluelles and Moore, at No. 1087; Baudouin and Jobin, at No. 377; Gaudet, at p. 332). But this does not mean that the contract never actually existed. Logically, a contract must exist before it can be annulled: if a contract did not become a legal reality, it cannot be deemed never to have existed, because it does not in fact exist. (…)[28]

[52] In the words of s. 137 *BIA*, the Respondent's claim "aris[es] out of [the] transaction" that was entered into between it and Bixi and was declared a nullity by the Court. Indeed, the Court's conclusion quoted above declares that the City may file a proof of claim in the amount of the balance due to it at the date of the taking in payment and not the balance due when the loan was declared a nullity.

[53] I conclude that it is an error of law to only consider the obligation of restitution and not the underlying transaction of 2011 in analyzing the Respondent's proof of claim.

[54] Given his view of the law, the judge did not consider whether the 2011 transaction was a proper transaction within the meaning of s. 137 *BIA*.

[55] The standard of review on appeal from a trustee's disallowance is correctness on questions of law and reasonableness (or palpable error) on questions of fact or mixed fact and law.[29] The parties had stipulated before the Superior Court that the only issue was the reasonableness of the Trustee's decision. That being said, the onus was on the Respondent in the lower court to demonstrate that the Trustee's decision was not reasonable.[30]

[56] As seen above, the Trustee found that the 2011 loan transaction was not proper because it was entered into in violation of a statutory provision of public order to protect taxpayers against misuse of public funds by municipalities. The Court agreed in the *2019 Judgment* and declared the loan agreement a nullity. Thus, it cannot be said that the Trustee's determination that the transaction was not proper was an unreasonable

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28 *Montréal (City) v. Octane Stratégie inc.*, 2019 SCC 57, [2019] 4 S.C.R. 138, para. 62.

29 *Sols Sportica inc. (Syndic de)*, 2016 QCCS 2109, paras. 26, 33, 39, Paquette J, aff'd, 2018 QCCA 504, leave to appeal to the SCC refused, 2019 CanLII 6031 (SCC). See also *Galaxy Sports Inc. (Re)*, 2004 BCCA 284, paras. 27-42.

30 *Alberta Energy Regulator v Lexin Resources Ltd*, 2018 ABQB 590, para. 72 [*Alberta Energy*].

conclusion. I would thus propose that the Court intervene to set aside the judgment and dismiss the appeal from the disallowance of the proof of claim.

4.- Did the judge err in concluding that the Trustee's determination that the Respondent's claim was an "equity claim" was unreasonable?

[57] Though not strictly necessary, given my opinion that the Trustee could postpone the Respondent's claim upon the application of s. 137 *BIA*, I propose to briefly examine the other ground in the disallowance, based on s. 140.1 *BIA,* to the effect that the "loan" was really a contribution to capital.

[58] The judge devoted two paragraphs to dismiss the Trustee's position in this regard:

> [37] Tout aussi téméraire l'argument subsidiaire que la créance devrait être également ajournée ne vertu de l'article 140.1 L.F.I. puisque la Ville serait un « Equity Partner » dans l'aventure commerciale de Vélo, puisqu'il fait fi des motifs développés tant par la Cour supérieure que par la Cour d'appel quant à l'aspect commercial de Vélo, limité à la seule aventure internationale et non pas quant au réseau strictement montréalais.
>
> [38] Cet argument ne tient pas compte non plus de l'ensemble de la preuve administrée devant la Cour supérieure alors que celle-ci constate que les gestes posés par la Ville ne visaient qu'à se faire rembourser les avances consenties par Société en commandite Stationnement de Montréal (SCSM) à Vélo, pour qu'elles lui soient versées à titre de redevances. En aucun temps il ne fut question d'une quelconque recherche de profits par la Ville.

[59] I reiterate that the standard of review of a trustee's disallowance is one of reasonableness.

[60] Equity claim is defined in s. 2 of the *BIA* as follows:

equity claim means a claim that is in respect of an equity interest, including a claim for, among others,	**réclamation relative à des capitaux propres** Réclamation portant sur un intérêt relatif à des capitaux propres et visant notamment :
(a) a dividend or similar payment,	a) un dividende ou un paiement similaire;
(b) a return of capital,	b) un remboursement de capital;
(c) a redemption or retraction obligation,	c) tout droit de rachat d'actions au gré de l'actionnaire ou de remboursement anticipé d'actions au gré de l'émetteur;

(d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or	d) des pertes pécuniaires associées à la propriété, à l'achat ou à la vente d'un intérêt relatif à des capitaux propres ou à l'annulation de cet achat ou de cette vente;
(e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d); (réclamation relative à des capitaux propres)	e) une contribution ou une indemnité relative à toute réclamation visée à l'un des alinéas a) à d). (equity claim)

[61] Was the 2011 loan a contribution by the Respondent to Bixi's capital?

[62] Judges sitting in bankruptcy matters have identified various indicia relevant to the examination:

> [41] ***U.S. Steel*** sets out a helpful two-part test in to be followed in situations involving parent-subsidiary relationships at paras 186-190:
>
> > (a) subjectively, did the alleged lender actually expect to be repaid the principle (sic) amount of the loan with interest out of the cashflows of the alleged borrower; and
> >
> > (b) objectively, was the expectation reasonable under the circumstances?
>
> [42] The Court in ***U.S. Steel*** referred to various factors used by American courts to aid in determining appropriate characterization, including the following:
>
> > (a) the names given to the instruments, if any, evidencing the indebtedness;
> >
> > (b) the presence or absence of a fixed maturity date and schedule of payments. The American cases suggest that the absence of a fixed maturity date and a fixed obligation to repay is an indication that the advances were capital contributions and not loans;
> >
> > (c) the presence or absence of a fixed rate of interest and interest payments. Again, it is suggested that the absence of a fixed rate of interest and interest payments is a strong indication that the advances were capital contributions rather than loans;
> >
> > (d) the source of repayments. If the expectation of repayment depends solely on the success of the borrower's business, the cases suggest that the transaction has the appearance of a capital contribution;
> >
> > (e) the adequacy or inadequacy of capitalization. Thin or inadequate capitalization is strong evidence that the advances are capital contributions rather than loans;

> (f) the identity of interest between the creditor and the shareholder. If shareholders make advances in proportion to their respective stock ownership, an equity contribution is indicated;
>
> (g) the security, if any, for advances;
>
> (h) the corporation's ability to obtain financing from outside lending institutions. When there is no evidence of other outside financing, some cases indicate that the fact no reasonable creditor would have acted in the same manner is strong evidence that the advances were capital contributions rather than loans;
>
> (i) the extent to which the advances were subordinated to the claims of outside creditors;
>
> (j) the extent to which the advances were used to acquire capital assets. The use of the advance to meet the daily operating needs for the corporation, rather than to purchase capital assets, is arguably indicative of bona fide indebtedness; and
>
> (k) the presence or absence of a sinking fund to provide repayments.[31]
>
> (Emphasis added)

[63] In *U.S. Steel*, Justice Wilton-Siegel underlined that in determining whether a transaction is a contribution to capital rather than a loan, the surrounding circumstances of the loan and the real intent of the parties rather than an adherence to the literal wording of a contract should be the focal point, particularly where the parties do not deal at arm's length.[32]

[64] The factual elements relied on by the Trustee and in evidence before the judge indicate the reasonableness of the Trustee's conclusion. The judge made no reference to these elements of proof in considering the application of s. 140.1 *BIA*.

[65] In 2011, Bixi was in a dire financial situation. Indeed, it was insolvent, having an operating deficit and no reasonable outlook for making up its deficit. The Respondent had no expectation that Bixi could ever repay the $31,000,000 in direct advance nor the $8,000,000 of the guaranteed loan. Without the Respondent's guarantee of that loan, Bixi could not find an operating lender and would be forced to cease its activities. The Respondent wanted Bixi to be able to continue to offer its bike sharing service to Montrealers. These are facts testified to by the CEO of Bixi as well as the Respondent's treasurer.

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31 *Alberta Energy*, *supra*, note 30, paras. 41-42.

32 *U.S. Steel Canada Inc. (Re)*, 2016 ONSC 569, para. 168.

[66] Under the 2011 agreement entered into by Bixi and the Respondent, the latter has all the hallmarks of a sole shareholder if not an *alter ego*, as described above in paragraph [45].

[67] I accept that the mere fact that a sole shareholder[33] (or group of shareholders)[34] advances funds to its company does not constitute *per se* a contribution to capital. However, the surrounding circumstances described above, taken together, make it such that the Trustee's determination that the loans were, in substance, contributions to capital was a reasonable determination. The judge erred by not considering the aforementioned facts and by not applying the appropriate standard of review in considering the Trustee's disallowance of the Respondent's proof of claim. This is a further ground justifying the Court's intervention.

* * *

[68] Accordingly, and for all the foregoing reasons, I would dismiss the application for leave to appeal without costs as it is not necessary given the right to appeal under s. 193 (c) *BIA*. I would then grant the appeal to set aside the judgment of the Superior Court and dismiss the Respondent's appeal from the Trustee's notice of disallowance, with legal costs before both courts.

[69] The Appellant also asks the Court to take cognizance that it has withdrawn its notice of disallowance regarding the sums of $6,489,081.12 and $1,702,600 representing the sums paid by the Respondent to National Bank of Canada pursuant to the guarantee for Bixi's liability to such bank. These amounts (totalling $8,191,681.12) are included in the total postponed amount of $39,938,256.12. The judge makes no mention that this alternative disallowance is overturned, but the Trustee, in its written pleadings in first instance, had withdrawn the disallowance of this portion of the claim in order that National Bank of Canada not continue to be a party to the proceedings. I propose to add such a conclusion to the Court's judgment.

MARK SCHRAGER, J.A.

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33 *Installations Doorcorp inc./Doorcorp Installations Inc. (Syndic d')*, 2012 QCCA 702, para. 55.

34 *Provost Shoe Shops Ltd. (Re)*, 1993 CanLII 4591, 21 C.B.R. (3d) 108 (NS SC).

TAB 25

Court of Queen's Bench of Alberta

Citation: Trakopolis SaaS Corp (2007996 Alberta Ltd) (Re), 2020 ABQB 643

Date: 20201022
Docket: B201 582159
Registry: Calgary

In the Matter of the Bankruptcy and Insolvency of Trakopolis SaaS Corp, also known as 2007996 Alberta Ltd.

In the Matter of the Bankruptcy and Insolvency of Trakopolis IoT Corp

Between:

ESW Holdings Inc

Applicant

- and -

The Trustee in Bankruptcy of the Estate of Trakopolis IoT Corp and the Estate of Trakopolis SaaS Corp

Respondent

Reasons for Decision
of the
Honourable Mr. Justice C.M. Jones

I. Introduction

[1] Alvarez & Marshall Canada Inc is the trustee in bankruptcy (the "Trustee") of the estates of Trakopolis IoT Corp ("IoT") and Trakopolis SaaS Corp ("SaaS").

[2] The Trustee disallowed claims submitted by ESW Holdings Inc ("ESW") on the grounds that they were equity rather than debt. ESW appeals those disallowances and asserts that the claims were grounded in debt, not equity.

[3] For the reasons set forth below, I dismiss ESW's appeal and uphold the disallowance of its claims. While I find that the guarantee in question does secure ESW's claims, I also find that they are equity claims.

II. Background

[4] On November 15, 2018, ESW advanced funds to IoT and SaaS (the "Lending Transaction") pursuant to a Loan and Security Agreement (the "LSA"). SaaS guaranteed IoT's obligations to ESW pursuant to a guarantee (the "SaaS Guarantee").

[5] According to ESW, the advance of funds to IoT was rejected by IoT's bank because the account to which ESW was attempting to transfer funds belonged not to IoT, but to SaaS. ESW claims it mistakenly understood that IoT was the operating company.

[6] To rectify this misunderstanding, ESW entered into an Amended and Restated Loan Agreement (the "ARLA") with IoT and SaaS dated November 27, 2018. SaaS and IoT also provided ESW with an executed acknowledgement (the "Acknowledgement") to confirm and acknowledge the continuing effect and enforceability of all existing "Security Documents", as that term was defined in the Acknowledgement.

[7] The ARLA required IoT to guarantee SaaS' obligations to ESW; that guarantee was effected on November 27, 2018 (the "IoT Guarantee"). Thus, both SaaS and IoT provided guarantees to ESW. The IoT Guarantee is not in issue in these proceedings.

[8] Upon execution of the ARLA and the Acknowledgement, the amounts that ESW had attempted to advance to IoT were advanced to SaaS.

[9] On or about December 20, 2019, 1234600 BC Ltd, a subsidiary of LLR Partners ("LLR"), entered into an asset purchase agreement (the "APA") with IoT and SaaS under which LLR purchased all tangible and intangible assets, property and rights of each of IoT and SaaS (the "Transaction"). The Transaction was completed on January 22, 2020.

[10] IoT and SaaS subsequently were assigned into bankruptcy (the "IoT Bankruptcy" and "SaaS Bankruptcy", respectively).

[11] On February 12, 2020, ESW submitted proofs of claim against IoT (the "IoT Claim") and against SaaS (the "SaaS Claim") (collectively, the "ESW Claim").

[12] On March 20, 2020, ESW received Notices of Disallowance for the IoT Claim (the "March 20 IoT Disallowance") and for the SaaS Claim (the "March 20 SaaS Disallowance"). In the March 20 IoT Disallowance, the Trustee concluded that the IoT Claim was an equity claim that was not entitled to any priority.

[13] In the March 20 SaaS Disallowance, the Trustee arrived at the same conclusion in respect of the SaaS Claim, but went further, advising ESW that:

> There is no evidence that was provided in the ESW 996 AB [SaaS] Claim that demonstrates an actual [SaaS Guarantee] exists. In the absence of an executed [SaaS Guarantee], it does not appear that Trak SaaS has any obligation to ESW pursuant to the Warrant.

[14] The Trustee ultimately acknowledged that executed copies of the SaaS Guarantee had been provided to it when the SaaS Claim was submitted.

[15] On March 29, 2020, the Trustee issued new Notices of Disallowance for the IoT Claim (the "March 29 IoT Disallowance") and for the SaaS Claim (the "March 29 SaaS Disallowance"). In these new disallowances, the Trustee maintained that the ESW Claim was an

equity claim**.** In the March 29 SaaS Disallowance, the Trustee also asserted that the SaaS Guarantee was excluded by the ARLA.

[16] ESW appeals these disallowances pursuant to s 135(4) of the *Bankruptcy and Insolvency Act*, RSC 1985, c B-3 ("*BIA*"), which contemplates an appeal to the Court from a trustee's disallowance of a claim against a bankrupt's estate. The Trustee asks this Court to dismiss the appeals and uphold each Notice of Disallowance.

III. Issues

[17] I accept ESW's articulation of the issues, as set out in its Brief:

1. The process for an appeal under s. 135(4) of the *BIA*;
2. The appropriate standard of review;
3. Whether ESW is permitted to introduce the Supplemental Evidence contained in the Affidavit of N. Gupta;
4. Whether the ESW Claim is an equity claim or a debt claim;
5. Whether the SaaS Guarantee secures obligations pursuant to the ARLA; and
6. Whether the ESW Claim ought to be approved.

[18] ESW's position on issues 1 through 3 is as follows:

1. An appeal under s. 135(4) of the *BIA* involves a *de novo* hearing, or, in its most restrictive formulation, a hybrid approach involving an appeal on the record and the admission of fresh evidence if the Court considers it warranted.
2. The appropriate standard of review is correctness.
3. The Supplemental Evidence is warranted.

[19] The Trustee did not oppose the admission of the Supplemental Evidence and took no position on whether this appeal should be heard *de novo* or as a hybrid appeal. If the appeal is to be heard as a hybrid appeal, the Trustee conceded that the appropriate standard of review is correctness.

[20] Thus, I need not determine issues 1 through 3. Further, the resolution of issue 6 will follow depending upon my assessment of issues 4 and 5.

IV. Analysis

A. Equity or Debt Claim

[21] Both the LSA and the ARLA contemplated conditions precedent to the advance of funds, one of which was delivery of a share purchase warrant.

[22] IoT and ESW entered into an agreement entitled "Warrant to Purchase Common Shares" (the "Warrant") which, among other things, gave ESW an option (the "Purchase Option") to purchase 1,307,620 common shares in IoT (the "Warrant Shares") at any point between November 15, 2018 and November 15, 2023 at a set price of $0.34 per common share.

[23] IoT agreed to purchase the Warrant for cancellation (the "Re-Purchase Payment Obligation"), at a price determined by formula, if an "Acquisition" occurred while the Purchase

Option remained outstanding. Acquisition is defined to include, *inter alia*, "the sale, exclusive license or other disposition of all or substantially all of the assets of IoT".

[24] ESW acknowledges that the "majority of amounts owing from IoT and SaaS to ESW were paid out as a result of the Transaction" but claims that the parties expressly agreed to defer a decision "on Trakopolis' obligations with respect to the Re-Purchase Payment Option".

[25] The price determination formula applicable to the Re-Purchase Payment Obligation is set forth in clause 1.6(c) of the Warrant as follows:

> In the event of an Acquisition, the Company [IoT] shall acquire from the Holder [ESW] effective immediately prior to and contingent upon the consummation of such Acquisition all of the Warrants then outstanding for an aggregate price equal to:
>
> A = B + C
>
> where:
>
> A = the aggregate consideration payable by the Company
>
> B = US $600,000 multiplied by X/1,307,620
>
> C = the greater of: (i) $0.00; or (ii) Y multiplied by (Z – Warrant Price) – B
>
> X = the number of Warrants that remain issued and unexercised at the time of the Acquisition, which figure shall be determined without making any adjustments pursuant to section 2 of this Warrant
>
> Y = the number of Shares issuable on exchange of all Warrants that remain issued and unexercised at the time of the Acquisition
>
> Z = the per Share value of the consideration payable to holders of Shares pursuant to the Acquisition, expressed in dollars.

[26] Based on this formula, ESW takes the position that the amount of the ESW Claim is US$600,000.

[27] While I will not undertake the algebraic exercise of computing ESW's claim pursuant to this formula, what is significant in my view is that the Re-Purchase Payment Obligation is decoupled from any outstanding loan amounts owed to ESW at the time of the Acquisition. Rather, it represents a negotiated amount determined with reference to the number of shares remaining to be issued at the time of the Acquisition, any amounts received by shareholders upon the Acquisition and the guaranteed payment amount.

[28] The central issue here is the proper interpretation of the rights and obligations arising under the Warrant. The Trustee took the position that the ESW Claim is an equity claim within s 140.1 of the *BIA*, which provides:

> A creditor is not entitled to a dividend in respect of an equity claim until all claims that are not equity claims have been satisfied.

[29] ESW asserts that the ESW Claim properly is classified as a debt claim arising from IoT's contractual obligations under the Warrant. ESW asserts that the Trustee incorrectly interpreted the true substance of the Warrant and erred in concluding that the ESW Claim is an equity interest.

1. Statutory Language

[30] The ESW Claim is in respect of the Warrant. The Trustee argues that the Warrant is an equity interest and that, therefore, the ESW Claim is an equity claim within the meaning of the *BIA* and is subordinated to the claims of secured and unsecured creditors.

[31] Two key definitions are found at s 2 of the *BIA*:

> **equity claim** means a claim that is in respect of an equity interest, including a claim for, among others,
>
> (a) a dividend or similar payment,
> (b) a return of capital,
> (c) a redemption or retraction obligation,
> (d) a monetary loss resulting from the ownership, purchase or sale of an equity interest or from the rescission, or, in Quebec, the annulment, of a purchase or sale of an equity interest, or
> (e) contribution or indemnity in respect of a claim referred to in any of paragraphs (a) to (d);
>
> **equity interest** means
>
> (a) in the case of a corporation other than an income trust, a share in the corporation — or a warrant or option or another right to acquire a share in the corporation — other than one that is derived from a convertible debt, and
> (b) in the case of an income trust, a unit in the income trust — or a warrant or option or another right to acquire a unit in the income trust — other than one that is derived from a convertible debt;

[32] It is important to note that the *BIA* was amended in 2009 to enact the above definitions. The Trustee points out that the words "in respect of" have been held by the Supreme Court of Canada to be words of the broadest scope that convey some connection between two subject matters: ***Nowegijick v The Queen***, [1983] 1 SCR 29 at p 39. ESW does not dispute that assertion.

[33] The Trustee asserts that the Warrant is not derived from a convertible debt and therefore falls within the definition of "equity interest". The Trustee argues that even if the Warrant can be said to be derived from a debt because it arose in connection with the LSA, the LSA did not create a convertible debt. No portion of any debt owed to ESW was converted or potentially convertible into equity, a warrant or a right to acquire equity.

[34] The Trustee asserts that the definition of equity claim encompasses the ESW Claim and cites ***Re Bul River Mineral Corp***, 2014 BCSC 1732 at para 82:

> Accordingly, while the 2009 amendments did represent in part a codification of the previous case law concerning equity claims, it also represented a more

> concrete definition of "equity claims" and by such definition a broadening and more expansive definition of such claims: ***Sino-Forest Corporation*** (ONCA) at paras. 24, 34-60. Parliament has now clearly cast the net widely in terms of the broad definition of equity claims such that claims that might have previously escaped such characterization will now be caught by the CCAA.

[35] The Trustee notes that the legislative amendments came into force after the cases relied on by ESW. Citing ***Sino-Forest Corporation (Re)***, 2012 ONCA 816 at para 53, the Trustee argues that the definition is sufficiently clear to alter the pre-existing common law.

[36] ESW acknowledges that under s. 140.1 of the *BIA*, a creditor is not entitled to a dividend respecting an equity claim until all claims other than equity claims have been satisfied. It argues, however, that it is not seeking a dividend and that it has never had an equity interest in IoT.

2. Fundamental Character of Relationship

[37] ESW argues that distinguishing a debt claim from an equity claim requires consideration of the overall effect of the transaction and the intention of the parties. It notes that the Court in ***Bul River*** at para 69 reaffirmed the importance of identifying the substance of a transaction and set out the following criteria for determining whether a claim is in debt or equity:

> (a) The fact that a transaction contains both debt and equity features does not, in itself, determine its characterization as either debt or equity;
> (b) The characterization of a transaction under review requires the determination of the intention of the parties;
> (c) It does not follow that each and every aspect of a "hybrid" debt and equity transaction must be given the exact same weight when addressing a characterization issue;
> (d) A Court should not too easily be distracted by aspects of a transaction which are, in reality, only incidental or secondary in nature to the main thrust of the agreement.

[38] ESW notes the Court's comments in ***Bul River*** at para 85:

> "[t]he 2009 amendments have not affected the ability of the court to continue to analyze the *substance* of the claims, albeit in the context of the expanded definition of "equity claim" [Emphasis in original.]

[39] ESW cites ***All Canadian Investment Corporation (Re)***, 2019 BCSC 1488 at para 43 for the proposition that the relevant test to distinguish between debt and equity claims is set out in ***Canada Deposit Insurance Corp v Canadian Commercial Bank,*** [1992] 3 SCR 558. The Court in ***All Canadian*** at para 69 quoted from ***CDIC*** at para 51:

> As in any case involving contractual interpretation, the characterization issue facing this court must be decided by determining the intention of the parties to the support agreements. This task, perplexing as it sometimes proves to be, depends primarily on the meaning of the words chosen by the parties to reflect their intention. When the words alone are insufficient to reach a conclusion as to the true nature of the agreement, or when outside support for a particular

> characterization is required, a consideration of admissible surrounding circumstances may be appropriate.

[40] While this statement is no doubt accurate, the 2009 amendments, without more, seem to constitute the Warrant an equity interest.

[41] In ***Canada Deposit***, the Supreme Court considered whether a warrant to purchase common shares created an equitable claim under the *BIA*. The Court noted at para 56 that the equitable nature of the warrant was merely incidental to its main purpose, which was to add incentive for the creditor to extend funds to the debtor:

> It is not without significance that none of the participants ever exercised any of their warrants nor did they assign them. In these circumstances, I agree with the Court of Appeal that the true effectiveness of the equity agreement was highly contingent and that the learned chambers judge erred in not considering the warrants for what they really were, namely, so-called "sweeteners" or "kickers" with respect to the advance of $255 million which were simply additional features to the underlying loan agreement between the parties. Undoubtedly, the warrants are an equity feature of the transaction supporting a conclusion that the advance was an investment. However, in the facts of this case, only minimal weight should be given to this factor in the overall characterization of the agreement.

[42] ESW argues that the Warrant was a "sweetener" or a "kicker" for ESW to extend credit. It asserts that the Re-Purchase Payment Obligation provided an alternative method to compensate ESW for extending credit at a reduced interest cost, compared to other lenders, and enabled IoT to retain more capital for its operations, while ensuring that ESW would be compensated in the event of an Acquisition.

[43] The Trustee argues that the Court in ***Canada Deposit*** considered the characterization of the loan as a whole. It did not consider either the warrants themselves or, as is the case here, a claim by a lender that also held warrants.

[44] The Trustee takes the position that issuance of an instrument in support of a loan transaction does not necessarily mean that the instrument is not equity. The Trustee asserts that the Warrant does not give rise to a debt claim merely because it was issued within a creditor-debtor relationship. Conceptually, there is nothing that prevents equity from being issued to a creditor in support of a loan transaction: ***Cirius Messaging Inc v Epstein Enterprises Inc***, 2018 BCSC 1859 at paragraph 75.

[45] Citing the discussion at para 24 of ***Sino-Forest*** at the Ontario Superior Court of Justice, the Trustee notes that shareholders have unlimited upside potential, while creditors do not. But for the insolvency, ESW's claim pursuant to the Warrant might have increased in value if the IoT shares had increased in value. Accordingly, the Trustee asserts that the ESW Claim is in substance, an equity claim.

3. Option Not Exercised

[46] On a related point, ESW asserts that it never held an "equity interest" because it did not exercise its option to purchase under the Warrant. ESW argues that its equity interest was contingent upon exercise of the Purchase Option.

[47] Citing ***Henderson v Minister of National Revenue***, [1975] CTC 485 at paras 30-31, ESW argues that it had no interest in the Warrant shares until it exercised the Purchase Option:

> However until subscription and allotment is made and communicated to the subscriber no shares come into existence. That being so the share purchase warrant does not confer rights on its holder in or over shares but only the right to have the shares issued….in relation to the warrants there were no shares in being.

[48] ESW's argument is that, without exercise of the Purchase Option, any equity features of the Warrant are incidental and do not change its true purpose, which was to provide additional consideration to ESW to extend credit to IoT. ESW notes that IoT agreed to purchase the Warrant for cancellation if an Acquisition occurred before ESW exercised the Purchase Option. Citing ***Henderson,*** it draws a distinction between share purchase warrants and share warrants.

[49] Notwithstanding that ESW did not exercise the Purchase Option, the Trustee disputes that ESW had no equitable interest in IoT and that the ESW Claim is not an equity claim. The Trustee argues that section 2 of the *BIA* clearly states that a warrant is an "equity interest" and makes no reference to whether it was acquired pursuant to the exercise of an option. Therefore, exercise of an option in respect of a share does not determine equitable status.

4. Disposition

[50] I find that the ESW Claim is an equity claim. The definition of equity interest in the *BIA* encompasses a warrant, option or another right to acquire a share in a corporation. The Warrant clearly conferred that right.

[51] But ESW points out that the Warrant conferred other rights. In the event of an Acquisition, IoT no longer had a contingent obligation to issues shares in its capital stock. Rather, it was obliged to acquire all outstanding Warrants for a price determined by formula. ESW contends that these are fundamentally different.

[52] I acknowledge that IoT's obligation upon an Acquisition was to pay money. But does it follow that ESW is therefore a "debtor" under the *BIA*? The Warrant arose in connection with a lending relationship. Had there been no loan arrangements, there would have been no Warrant. In my view, however, that connection does not make the *substance* of the Warrant, and the rights and obligations arising thereunder, debt rather than equity.

[53] Certainly, the loan arrangements gave rise to a debtor-creditor relationship. But it was a term of those lending arrangements that ESW be given the right to acquire equity. IoT's obligation to make payment in the event of an Acquisition stands in substitution for its obligation to issue shares.

[54] ESW claims it secured the right to acquire shares of IoT partly in consideration for extending more favourable lending terms. But it was still a right to acquire shares. Clearly, had matters evolved as ESW hoped, it would have become a shareholder of IoT and enjoyed the "upside" devolving from appreciation in the value of IoT and its stock. That "upside" did not take the form of a higher interest rate or any other characteristic of a lending transaction. Rather, it would have represented a fundamental alteration in the relationship between the parties.

[55] ESW asserts in its brief that the Re-Purchase Payment Obligation provided "real and tangible value to IoT and SaaS as an alternative method of compensating ESW for providing funding with reduced ongoing interest costs relative to that offered by other lenders".

[56] That may be, but if a lender receives two forms of consideration - interest and an option to acquire shares - and the latter is to some extent in lieu of the former, rights arising under the latter do not necessarily have the character of debt. The lending arrangements and Warrant are not so closely related that the Warrant can be viewed simply as an extension or attribute of those lending arrangements.

[57] I am bolstered in my conclusion by the terms of the formula applicable to the Re-Purchase Payment Obligation. That formula, as noted above, makes no reference to amounts borrowed from ESW, whether outstanding or not. Rather, IoT's payment obligation is computed with reference to shares and their value. That being the case, I conclude that the computation reflects an intention to provide an investment return to ESW rather than a debt repayment.

[58] I think it necessary to look at the Warrant as a whole and not to parse its components. But even if I consider the Re-Purchase Payment Obligation on a "stand alone" basis, does that represent a distinct debtor-creditor relationship? Can the Warrant be viewed as a contract that confers different rights in different circumstances? For several reasons, I think that is the wrong approach.

[59] At a high level, I do not think it serves the interests of commercial certainty to allow the nature of a party's claim to a bankrupt entity's estate to undergo a paradigm shift from equity to debt. To do so would, I believe, introduce an element of uncertainty in the expectations of lenders and investors who want to enter into transactions knowing what rights are claimed by other stakeholders. I think there is commercial merit to requiring parties to "pick their ponies" at the outset.

[60] That said, I note the exception for convertible debt in paragraph (d) of the definition of equity claim. What starts out as debt remains debt, even if a conversion right to equity is exercised.

[61] But the reverse is not true. The definition of equity interest does not exclude from its ambit an equity interest that has converted to debt. Had Parliament intended to exclude such converted claims from the definition of equity interest, it could have done so expressly as it did with convertible debt.

[62] Indeed, in my view, precisely the opposite perspective is reflected in the definition of equity claim. Amounts substituted for rights otherwise conferred by a share (return of capital, proceeds of redemption or retraction) are specifically defined as equity claims. The Warrant contemplates substitution of the right to receive cash for what clearly would have been an equity claim.

[63] Further, the parties acknowledge that the words "in respect of" in the definition of "equity claim" are to be construed broadly. There must be some connection between the claim asserted and an equity interest.

[64] The Warrant creates that connection. ESW's right to demand a cash payment would not have arisen were it not for the Warrant, which is clearly defined as an equity interest.

[65] In my view, the totality of the circumstances establishes that the Warrant is an equity interest. Accordingly, the ESW Claim pursuant to the Warrant is an equity claim.

B. SaaS Guarantee

[66] Given my finding that the obligation under the Warrant that is secured by the SaaS Guarantee is an equity claim, the Trustee asserts that it is therefore moot whether or not the SaaS Guarantee is enforceable in respect of the ESW Claim.

[67] It may be unnecessary to consider the effects of the SaaS Guarantee, the ARLA and the Acknowledgement. Clearly, ESW's claim pursuant to the SaaS Guarantee cannot enjoy a higher priority than the obligations under the Warrant secured by the SaaS Guarantee. However, if I am incorrect in concluding that the ESW Claim is an equity claim, the enforceability of the SaaS Guarantee becomes relevant. Accordingly, for completeness, I consider whether the SaaS Guarantee secures obligations pursuant to the ARLA.

1. Sale Approval and Vesting Order

[68] This Court granted a Sale Approval and Vesting Order in respect of the Transaction. ESW asserts that it was negotiated specifically among counsel that the Sale Approval and Vesting Order would discharge only the security granted by SaaS to ESW as it related to the assets described in the APA and that, in other respects, the security would remain valid and in full force and effect. ESW maintains that it never released the obligations pursuant to the SaaS Guarantee or IoT Guarantee.

[69] The Trustee has not challenged this assertion and I consider it unnecessary to examine it further because the Sale Approval and Vesting Order provides that those asserting claims against IoT and SaaS may look only to the net proceeds of sale of their assets.

2. The Lending Transaction

[70] The logical approach to resolving this issue is to determine first what obligations were secured initially by the SaaS Guarantee. Then, I will consider to what extent, if any, the ARLA and Acknowledgement changed that security.

[71] As will quickly become apparent, the precise scope of the security arrangements depends upon a series of definitions nested like Russian dolls in the various agreements.

a. The SaaS Guarantee

[72] I begin with the SaaS Guarantee itself. The recitals thereto identify IoT as the "Borrower" and state that SaaS agrees to guarantee payment of "Guaranteed Obligations" to ESW. Guaranteed Obligations are stated in Recital B to be "the Obligations of [IoT] to ESW under the Loan and Security Document, or any other Loan Documents".

[73] The reference to "Loan and Security Document" appears to be an error as that term is neither defined nor used elsewhere. I believe it was intended to be a reference to the LSA. Consequently, to understand what SaaS guaranteed, it is necessary to understand IoT's obligations to ESW under the LSA.

[74] Paragraph 1.1 of the SaaS Guarantee defined the LSA to be:

> …the loan and security agreement made as of the date hereof among, *inter alia*, the Lender and the Borrower, as the same may be amended and restated, modified or replaced from time, to time, and pursuant to which the Lender established certain credit facilities in favour of the Borrower.

[75] Further, paragraph 1.2(e) of the SaaS Guarantee provides as follows:

> Except as otherwise provided in this Guarantee, any reference to this Guarantee, the Loan and Security Agreement or any of the Loan Documents refers to this Guarantee, the Loan and Security Agreement or such Loan Documents as the same may have been or may from time to time be amended, modified, extended, renewed, restated, replaced or supplemented and includes all schedules to it.

[76] Thus, the Guaranteed Obligations that SaaS agreed to guarantee consisted of IoT's obligations to ESW not only under the LSA, but also under other Loan Documents. Recital B to the SaaS Guarantee makes it clear that Loan Documents means something more than just the LSA.

[77] The introductory language in paragraph 1.1 of the SaaS Guarantee provides as follows:

> Except as otherwise expressly provided herein, capitalized terms in this Guarantee (including the Recitals hereto) but not defined herein shall have the meanings assigned to such terms in the Loan and Security Agreement.

b. The LSA

[78] Therefore, I now turn to the LSA to understand the meaning of Loan Documents as well as what obligations IoT had under those Loan Documents and the LSA. That, in turn, determines what SaaS agreed to guarantee.

[79] Exhibit A to the LSA contains definitions. "Obligations" is defined as:

> All debt, principal, interest, Lender Expenses, fees, the Prepayment Premium, if any, *and other amounts owed to Lender by the Borrower [IoT] pursuant to this Agreement or any other agreement, whether absolute or contingent, due or to become due, now existing or hereafter arising,* including any interest that accrues after the commencement of an Insolvency Proceeding and including any debt, liability, or obligation owing from Borrower to others that Lender may have obtained by assignment or otherwise. [Emphasis added.]

[80] The definition of "Loan Documents" is as follows:

> this Agreement [LSA], the Confidentiality Agreement, the Expenses Agreement, the Intellectual Property Security Agreement, the Guarantee, the General Security

> Agreement, the Pledge Agreement, the Control Agreement, note or notes executed by the Borrower [IoT] and Guarantor [SaaS], *and any other document, instrument or agreement entered into in connection with this Agreement or the Obligations, all as amended or extended from time to time*. [Emphasis added.]

[81] The Warrant stated this under the heading "Credit Facility":

> This Warrant to Purchase Common Shares ("Warrant") is issued *in connection* with that certain Loan and Security Agreement of even date herewith between ESW Holdings Inc. and the Company [IoT] (as amended and/or modified and in effect from time to time, the "Loan Agreement"). [Emphasis added.]

[82] In my view, the italicized portion of the definition of "Obligations" operates to include amounts that may become owing to ESW by IoT under the Warrant on Acquisition. Thus, IoT's obligation to make a payment to ESW under the Warrant in the event of an Acquisition was an Obligation of IoT to ESW under the LSA and the Warrant. As such, at the time of the Lending Transaction, the SaaS Guarantee extended to that Obligation.

3. ARLA and Acknowledgement

[83] The Trustee does not appear to take issue with this. Rather, its arguments are focused on the effect of the ARLA and, more particularly, the Acknowledgement. Therefore, I now consider how the ARLA and the Acknowledgement may have affected the application of the SaaS Guarantee to IoT's Obligation to make payment to ESW under the Warrant.

a. The ARLA

[84] The second recital to the ARLA provides as follows:

> AND WHEREAS Trak IoT has requested and Lender has agreed to amend and restate, *without novation*, the terms and conditions of the Original Loan Agreement on and subject to the terms contained herein. [Emphasis added.]

[85] Counsel were unable to clarify the intended meaning of the words "without novation" but nothing appears to turn on it.

[86] In any event, the ARLA purports to amend and restate the LSA. As with the LSA, delivery of the Warrant to ESW was a condition precedent to the loan to IoT.

[87] There was another condition precedent of note. Clause 3.1(g) required a Guarantee be provided by each "Guarantor", which was defined to include IoT and Trakopolis US, but not SaaS because SaaS was now the Borrower under the ARLA. While, taken by itself, this might appear to relieve SaaS of the obligation to guarantee IoT's contingent payment to ESW under the Warrant, there are further considerations.

[88] Both parties made arguments in respect of the "Entire Agreement" clause at clause 12.14 of the ARLA:

> This Agreement and the other Loan Documents embody the entire agreement and understanding between the parties hereto and thereto and supersede all prior

> agreements and understandings between such parties relating to the subject matter hereof and thereof and may not be contradicted by evidence of prior or contemporaneous agreements of the parties. There are no unwritten oral agreements between the parties related to the subject matter of this Agreement and the other Loan Documents. Notwithstanding the foregoing, the Canadian Credit Parties [SaaS and IoT] acknowledge and confirm and agree that the execution and delivery of this Agreement does not, and shall not, in any way be deemed to be a novation of the Original Credit Agreement or any accommodations of credit provided to Borrower prior to the date hereof. Each Canadian Credit Party [SaaS and IoT] hereby further acknowledges and agrees that any of the Loan Documents granting a Lien in any of the Collateral of the Canadian Credit Parties [SaaS and IoT] shall continue to guarantee and secure all of the Obligations and that the guarantees provided by, and the Liens granted under, such Loan Documents shall not be limited, terminated or discharged by the execution and delivery of this Agreement.

[89] ESW asserts that the "Entire Agreement" clause contemplates additional documents and instruments in support of the ARLA. It points to the expansive definitions of "Loan Documents" and "Obligations" in support of its position that the SaaS Guarantee is a security instrument that secures Obligations, as that term is defined under the ARLA. This means, ESW argues, that the SaaS Guarantee was not terminated, altered, amended or discharged by the ARLA.

[90] ESW argues that it is not commercially reasonable to think that it would have entered into the ARLA without the security of the SaaS Guarantee, which was signed only two weeks earlier. It cites ***Resolute FP Canada Inc v Ontario (Attorney General)***, 2019 SCC 60 at paras 142-3:

> …commercial reasonableness is a crucial consideration in interpreting a contract (see *Canadian Contractual Interpretation Law*, at p. 55). This is simply a corollary of the object of discerning the parties' intentions: when interpreting commercial contracts, courts seek to reach a commercially sensible interpretation, since doing so is more likely than not to give effect to the intention of the parties…
>
> Discerning commercial reasonableness entails, like all contractual interpretation, an objective analysis (see *Canadian Contractual Interpretation Law*, at p. 57) Courts should therefore read commercial contracts in a "positive and purposive manner", seeking to understand the structure of the agreement reached by the parties, the purpose of the transaction and the business context in which the contract was intended to operate.

[91] ESW argues that the language and commercial purpose of the ARLA objectively indicate the parties' intention that the SaaS Guarantee secure obligations under the ARLA, including IoT's obligation to make a payment under the Warrant.

[92] The Trustee argues that the term Loan Documents does not extend to the SaaS Guarantee, which was executed by SaaS in support of IoT's obligations to ESW. Since IoT has repaid its loan from ESW, it is no longer has any obligation to ESW and there are no grounds for ESW to pursue SaaS for repayment of any indebtedness owing by IoT to ESW. The Trustee argues that the SaaS

Guarantee is therefore "invalid" and that the language in the Acknowledgement and the ARLA does not render it operative.

[93] ESW argues that the Trustee's interpretation of the Entire Agreement clause is contrary to principles of contractual interpretation. It cites ***Tercon Contractors Ltd v British Columbia (Minister of Transportation & Highways)***, 2010 SCC 4 at para 64:

> The key principle of contractual interpretation here is that the words of one provision must not be read in isolation but should be considered in harmony with the rest of the contract and in light of its purposes and commercial context.

[94] The Supreme Court noted that an exclusion clause must be considered in light of its purpose and commercial context, as well as its overall terms.

[95] ESW argues that the only commercially reasonable interpretation consistent with the language and commercial purpose of the ARLA and the surrounding circumstances is that the ARLA incorporates the SaaS Guarantee as security for IoT's obligations.

[96] I find the Trustee gives an overly restrictive interpretation to what SaaS was purporting to guarantee under the SaaS Guarantee. Notwithstanding that IoT had paid back its loan from ESW, it had obligations under the Warrant. The SaaS Guarantee extended to IoT's contingent obligation to make a payment to ESW under the Warrant in the event of an Acquisition.

[97] Loan Documents was defined in the ARLA to include not only the Guarantees, but also "any other document, instrument or agreement entered into in connection with this Agreement [ARLA] or the Obligations, all as amended or extended from time to time." While the SaaS Guarantee was not entered into in connection with the ARLA, it was entered into in connection with the "Obligations", which include, *inter alia*, "other amounts owed to [ESW] by [SaaS] pursuant to…any other agreement, whether absolute or contingent, due or to become due, now existing or hereafter arising…". The phrase "any other agreement" reasonably may be interpreted to include the SaaS Guarantee. Therefore, I find that the SaaS Guarantee was executed "in connection" with the ARLA and is included in the term Loan Documents.

[98] Additionally, the Trustee argues that even if the SaaS Guarantee is a "Loan Document" under the ARLA, it is not a Loan Document "granting a Lien in any of the Collateral of [SaaS] and [IoT]". As such, the SaaS Guarantee is not captured by the Entire Agreement clause stating that Loan Documents shall not be terminated or discharged by the ARLA. The result, the Trustee alleges, is that the SaaS Guarantee became ineffective when the parties entered into the ARLA.

[99] I have already found that the SaaS Guarantee is a Loan Document. Both the LSA and the ARLA contain the same definitions of "Lien" and "Collateral".

[100] A Lien means any mortgage, lien, deed of trust, charge, pledge, security interest or other encumbrance. Exhibit B of the ARLA describes Collateral as including "all personal property of SaaS of every kind, whether presently existing or hereafter created or acquired, and wherever located…". It then goes on to describe various classes of property included in the meaning of Collateral.

[101] Clause 3.13 of the SaaS Guarantee provides that:

> The Guarantor [SaaS] acknowledges that this Guarantee is intended to secure payment and performance of the Guaranteed Obligations and that the payment and performance of the Guaranteed Obligations and the other Obligations of the Guarantor under this Guarantee are secured pursuant to the terms and provisions of the Guarantor Security Documents.

[102] Guarantor Security Documents are defined in the SaaS Guarantee to mean:

> The general security agreement dated as of the date hereof and any other security executed and delivered by the Guarantor to and in favour of the Lender, from time to time in respect of the Guarantee Obligations.

[103] The general security agreement between SaaS and ESW (the "GSA") defines Collateral to mean:

> All undertaking, personal property and assets of the Debtor (SaaS) now owned or hereafter acquired and any proceeds from the sale or other disposition thereof, all of which is further described, without limitation, in Section 2.02.

[104] Thus, all of SaaS' property constitutes Collateral. Clause 2.01 of the GSA provides that:

> As general, continuing and collateral security for the payment and performance of all Obligations, the Debtor (SaaS) hereby grants to the Lender (ESW) a security interest in the Collateral.

[105] The Trustee cannot argue a misalignment between the "Borrower" and the "Debtor" under the GSA, as it does under the ARLA. The GSA identified IoT as the "Borrower" and SaaS as the "Debtor".

[106] Clause 4.2 of the SaaS Guarantee provides as follows:

> Until the Guaranteed Obligations and all other amounts owing under this Guarantee are indefeasibly paid and performed in full and the Lender has no Guaranteed Obligations under the Loan and Security Agreement or the Loan Documents, the Guarantor covenants and agrees that:
>
> …
>
> (b)it will not surrender or lose possession of, sell encumber, lease, rent, or otherwise dispose of or transfer any of its real or personal property or right or interest therein, other than in the ordinary course of business consistent with past practice without the prior written consent of the Lender; and
>
> (c) it will not incur, issue or make any request for or permit to exist any further indebtedness to any third party, other than debt secured by Permitted Encumbrances under the Loan and Security Agreement and unsecured trade debt incurred in the ordinary course of business consistent with past practice or any contingent liabilities in connection with contracts entered into in the ordinary course of business, without the prior written consent of the Lender.

[107] I am satisfied that clauses 3.13 and 4.2 of the SaaS Guarantee grant a lien, charge, pledge, security interest or other encumbrance over SaaS' assets, which constitute Collateral.

[108] Pursuant to the Entire Agreement clause, whatever else the ARLA did, it did not affect the operation of the Loan Documents, in so far as those Loan Documents granted a Lien in the Collateral of IoT and SaaS. Accordingly, I find that the ARLA provided for continued recognition of the SaaS Guarantee in support of IoT's obligation to pay amounts to ESW in the event of an Acquisition.

[109] The SaaS Guarantee forms part of the understanding between SaaS and ESW reflected in the ARLA. I reject the Trustee's argument to the contrary.

b. The Acknowledgement

[110] As noted above, the ARLA became necessary because of a misunderstanding regarding the respective roles of IoT and SaaS. The lending agreements that had been implemented did not correctly identify the entity vested with operations and Canadian assets. Under the ARLA, SaaS and IoT acknowledged that the security granted under the LSA, including the SaaS Guarantee, would continue to be valid and enforceable. To underscore that point, they entered into the Acknowledgement, the recitals to which refer to the LSA and ARLA.

[111] SaaS is identified as the Borrower in the Acknowledgement. SaaS and IoT are the "Obligors".

[112] Recital C provides, *inter alia*, as follows:

> As security for the indebtedness, liabilities and obligations of the Borrower [Saas] to the Lender, the Lender has required that the Obligors [IoT and SaaS] execute and deliver certain security agreements, instruments and documents, and other agreements (collectively, as amended, restated supplemented or replaced, the "Security Documents"), including, without limitation, general security agreements from each of the Obligors, a share pledge agreement from the Borrower granting a security interest in the shares of Trakopolis USA Corp. and an assignment of insurance from the Obligors.

[113] Recital D provides as follows:

> Each of the Obligors have entered into this agreement to acknowledge and confirm the continuing enforceability and effect of all existing Security Documents.

[114] The Trustee argues that the SaaS Guarantee was granted as security for the indebtedness, liabilities and obligations not of SaaS, but of IoT. Therefore, it cannot be a "Security Document" because that definition captures only security for the indebtedness, liabilities and obligations of SaaS. This renders the SaaS Guarantee ineffective and excludes it from the ARLA.

[115] ESW argues that the SaaS Guarantee was always intended to secure IoT's obligations under the ARLA. It argues that the Trustee was incorrect to conclude that the SaaS Guarantee did not exist or that the ARLA excludes the SaaS Guarantee.

[116] ESW asserts that the surrounding circumstances, especially the Acknowledgement, demonstrate the parties' objective intention for the SaaS Guarantee to secure obligations under the ARLA. It cites ***Nexstep Resources Ltd v Talisman Energy Inc***, 2012 ABQB 62 at para 6:

> Thus, the authorities give guidelines for the consideration of the "factual matrix" or "surrounding circumstances" to help determine the parties' contractual intention as would be determined by a reasonable person so situated. In other words, extra-textual evidence is used to help understand what the parties meant by the words they used.

[117] ESW argues that the Acknowledgement is such "extra-textual evidence" in that it is an express statement of the parties' intentions for the SaaS Guarantee to secure IoT's obligations under the ARLA.

[118] Pursuant to s. 3.1(r) of the ARLA, the extension of credit under the ARLA was conditional upon any documents or certificates that ESW deemed necessary. ESW's evidence is that it required IoT and SaaS to enter into the Acknowledgement before it would agree to the ARLA.

[119] In the Acknowledgement, IoT and SaaS acknowledged and confirmed the continuing effect and enforceability of all security documents that existed at the time the LSA was executed. Since the SaaS Guarantee existed at the time of the LSA, ESW asserts that it is included under the Acknowledgement.

[120] In my view, the Trustee interprets Recital C too narrowly. I find that SaaS' obligations and liabilities to ESW included its undertaking, "secured" by the SaaS Guarantee, to guarantee performance of IoT's contingent obligation under the Warranty to pay an amount to ESW in the event of an Acquisition.

[121] I think it reasonable to interpret the term "obligations of the Borrower" to include SaaS' obligation under the SaaS Guarantee to secure IoT's obligation to make payment under the Warrant. It is clear that SaaS guaranteed IoT's obligations under the Warrant in the LSA. The later arrangements reflecting SaaS as the Borrower did not operate to change that understanding.

[122] Therefore, I find that the SaaS Guarantee is a Security Document. Recital D of the Acknowledgement confirms its enforceability post-LSA, under the ARLA.

[123] That enforceability is further confirmed in clause 2 of the Acknowledgement:

> The Security Documents shall continue in full force and effect as general continuing security for any and all indebtedness, liabilities and obligations of each of the Obligors to the Lender, including, without limitation, under, in connection with, relating to the Loan Agreement, and the security interests created by the Loan Documents shall charge the property of the Obligors in accordance with terms thereof.

[124] Accordingly, had I not found that the ESW Claim is an equity claim, I would have found that the SaaS Guarantee was validly issued and enforceable in support the ESW Claim.

V. Conclusion

[125] In the result, ESW's appeal is dismissed.

[126] I wish to thank the parties and, in particular, counsel for ESW, for their excellent and original material.

Heard on the 18th day of August, 2020.
Dated at the City of Calgary, Alberta this 22nd day of October, 2020.

C.M. Jones
J.C.Q.B.A.

Appearances:

William Skelly, Catrina Webster and Kaitlin Ward
for the Applicant

Mihai Tomos
for the Respondents

TAB 26

CITATION: YG Limited Partnership (Re), 2022 ONSC 6138
COURT FILE NO.: BK-21-02734090-0031
DATE: 20221101

SUPERIOR COURT OF JUSTICE – ONTARIO
IN BANKRUPTCY AND INSOLVENCY
(COMMERCIAL LIST)

RE: IN THE MATTER OF *THE BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, c. B-3, AS AMENDED
IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF YG LIMITED PARTNERSHIP AND YSL RESIDENCES INC.

BEFORE: Kimmel J.

COUNSEL: *Robin Schwill and Chenyang Li*, for the Proposal Trustee, KSV Restructuring Inc.

Jason Berall, for the Proposal Sponsor, Concord Properties Developments Corp.

Alexander Soutter, for Yonge SL LPs

Shaun Laubman, for Chi Long LPs

Mark Dunn and Sarah Stothart, for Maria Athanasoulis

HEARD: October 17, 2022

ENDORSEMENT
(FUNDING MOTION)

Overview

[1] YG Limited Partnership and YSL Residences Inc. (together, "YSL" or the "Debtor") filed Notices of Intention to Make a Proposal under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 (the "*BIA*"), which were procedurally consolidated pursuant to an Order dated May 14, 2021. The Debtor companies are special purpose entities established to hold the assets for a large real estate development in downtown Toronto known as the "YSL Project".

[2] This court approved an Amended Third Proposal dated July 15, 2021 (the "Proposal") on July 16, 2021. Under the Proposal, the moving party, KSV Restructuring Inc. (the "Proposal Trustee"), was authorized to deal with various claims against the Debtor, some of which were disputed.

[3] In the Proposal, Concord Properties Developments Corp. (the "Sponsor") covenanted in sections 10.2 and 11.1 to indemnify the Proposal Trustee for "all Administrative Fees and

Expenses (defined below) *reasonably incurred* [and not covered by the reserve established on the Proposal Implementation Date by the Sponsor in respect of the reasonably estimated additional Administrative Fees and Expenses anticipated to be incurred in connection with the administration of Distributions, resolution of any unresolved Claims … and the Proposal Trustee's discharge]". [emphasis added]

[4] "Administrative Fees and Expenses" are defined in the Proposal as "the fees, expenses and disbursements incurred by or on behalf of the Proposal Trustee, the solicitors for the Proposal Trustee, the solicitors of the Company both before and after the Filing Date."

[5] The Proposal Trustee brings this motion to compel the Sponsor to provide funding for the Proposal Trustee's continuing work towards the determination and/or resolution of the outstanding proofs of claim against the Debtor.[1] Jurisdictional questions have been raised within the motion.

[6] For reasons given orally at the hearing, I declined to grant the contested adjournment of this motion that the Sponsor asked for at the outset.

[7] For the reasons that follow, I have concluded that the Sponsor is not obligated to fund phase 2 of the Arbitration that was intended to determine the Athanasoulis Claim (as those terms are later defined herein). The Sponsor is obligated to indemnify the Proposal Trustee for its Administrative Fees and Expenses reasonably incurred to determine that claim itself, with the benefit of the Award from phase 1 of the Arbitration. The specific orders and directions arising from this ruling are detailed in this endorsement.

Background to the Motion

[8] As of October 2022, most of the claims filed against the Debtor had been settled or accepted by the Proposal Trustee. The largest claim, by far, filed against the Debtor is made by Maria Athanasoulis. This claim is comprised of $1 million for wrongful dismissal damages and $18 million in damages for alleged breaches of an oral profit-sharing agreement by which she alleges YSL must pay her 20% of the profits earned on the YSL Project (the "Athanasoulis Claim").

[9] The Athanasoulis Claim is one of three disputed claims by various stakeholders that the Proposal Trustee says have increased the professional costs associated with the Proposal and prevented the Proposal Trustee from completing the administration of these proceedings.

[10] As of the end of July 2022, the Proposal Trustee's Administrative Fees and Expenses totalled just under $1.2 million, excluding Harmonized Sales Tax. Included in that total were the costs of phase 1 of an arbitration held from February 22-25, 2022 (the "Arbitration") before William G. Horton ("the Arbitrator"). The Proposal Trustee and Ms. Athanasoulis both

[1] The motion originally sought the determination of the Sponsor's obligation to fund certain past expenses incurred by the Proposal Trustee; however, these expenses have been funded through previous advances from the Sponsor and the Sponsor advised that it is not seeking to "claw-back" monies previously advanced nor challenge the use of funds by the Proposal Trustee to date. Thus, the practical implication of this motion is only to deal with future funding obligations of the Sponsor.

participated in the Arbitration. It resulted in a partial award dated March 28, 2022 (the "Arbitration Award") that included findings that:

a. The Debtor had entered into an oral profit sharing agreement with Ms. Athanasoulis;

b. Ms. Athanasoulis was an employee of YSL; and

c. Ms. Athanasoulis was constructively dismissed by YSL in December 2019.

[11] The Proposal Trustee says that it agreed to arbitrate the Athanasoulis Claim because the existence of the oral profit sharing agreement upon which it was based, as well as Ms. Athanasoulis' status with the Debtors (and other entities within the same corporate group referred to as the Cresford Group), were disputed by the Debtor's representative(s) and the determination of those questions would turn on credibility assessments. In these circumstances, the Proposal Trustee believed that the determination of whether Ms. Athanasoulis had a profit sharing agreement, what its terms were and whether she was an employee who was constructively dismissed, could be best determined through a hearing with *viva voce* evidence.

[12] The Sponsor was told on December 1, 2021 "that arrangements are being made with [Mr.] Horton to arbitrate the claim in late February, which is the earliest available date."

[13] The terms of appointment of the arbitrator were signed by the Proposal Trustee and Ms. Athanasoulis on December 9, 2021 (the "Agreement to Arbitrate"). By its terms, the parties agreed to:

a. appoint Mr. Horton to serve as sole arbitrator of their dispute relating to the Athanasoulis Claim; and

b. bifurcate the Athanasoulis Claim such that the Arbitration shall initially resolve only the liability of YSL (in phase 1). In the event the Arbitrator finds that YSL is liable to Ms. Athanasoulis, the parties agreed to schedule an additional hearing before the Arbitrator to determine the quantum of YSL's liability (in phase 2).

[14] The Sponsor did not receive a copy of the Agreement to Arbitrate at that time and was not privy to its specific terms.

[15] The Proposal Trustee was advised on March 31, 2022 that "[w]e received the decision in the fact finding phase just the other day or so. Arbitrator Horton found an enforceable 20% profit sharing agreement to exist."

[16] A few weeks later, the Proposal Trustee provided the Sponsor an updated budget. With only approximately $210,000 remaining from the original reserve established under s. 10.1 of the Proposal, the Proposal Trustee requested additional net funds of approximately $1.485 million in respect of Administrative Fees and Expenses anticipated to be incurred in connection with the resolution of the remaining three claims and to administer the distributions.

[17] Some limited partners of YSL (the Yonge SL LPs and Chi Long LPs, collectively the "LPs") questioned the Proposal Trustee's handling of certain disputed claims, including the Athanasoulis Claim. The LPs are entitled to any remaining cash in the $30.9 million "Affected Creditors Cash Pool" established by the Sponsor, after proven claims are paid out. That cash pool is only to be used by the Proposal Trustee to satisfy proven claims. Therefore, the determination of the Athanasoulis Claim could impact the LPs' recovery from the Affected Creditors Cash Pool.

[18] At a case conference on May 24, 2022, the LPs asked the court to schedule motions they proposed to bring. Their motions were described at that time to be directed to the Proposal Trustee's authority to arbitrate the Athanasoulis Claim and to determine whether the Athanasoulis' Claim is subordinate to the LPs' entitlements. They also requested that the court order a stay of phase 2 of the Arbitration of the Athanasoulis Claim. At that time, the authority of the Proposal Trustee to enter into the Agreement to Arbitrate was being challenged by at least one of the LPs.

[19] Instead of scheduling that motion, the court urged the parties to work out an arrangement that would allow the LPs' priority claims to be added to, and determined in, the existing Arbitration under an expanded comprehensive arbitration process (the "consolidated arbitration process").[2]

[20] At a further case conference on June 8, 2022, the parties updated the court about their ongoing discussions since the last case conference. The LPs indicated that they would be prepared to have their priority issues determined in a consolidated arbitration process. The Sponsor expressed concerns about the added cost of adding the LPs priority issues into the existing Arbitration process. The Sponsor asked for two conditions: i) that there be an attempt to settle through mediation before embarking upon stage 2 of the Arbitration and/or any consolidated arbitration process, and ii) that the LPs undertake to pay the Proposal Trustee's expenses associated with the next phase of the consolidated arbitration process. The LPs did not agree to either of these conditions.

[21] The court once again urged the parties to continue collaborating and refining the issues for a potential consolidated arbitration process and to try to reach an agreement about the additional cost of this expanded arbitration of all issues, in the face of the alternative of parallel proceedings and the added cost and delay that would ensue if the LPs' proposed motion was scheduled. The court summarized the outstanding issues to be addressed (or not to be addressed) in the context of a potential consolidated arbitration process and some of the terms that were under consideration, as had been identified by the parties at that time, in an endorsement dated June 8, 2022 as follows:

> a. The enforceability of the contract as found by Mr. Horton regarding Ms. Athanasoulis' claim and the quantum of any damages she may have suffered.

[2] This reference to a "potential consolidated arbitration process" is not intended to resolve the dispute between Ms. Athanasoulis (and the Proposal Trustee), on the one hand, and the LPs on the other, about whether they did in fact reach an agreement to consolidate all issues into an arbitration. That issue was not squarely put before the court on this motion.

b. Whether any claim for damages by Ms. Athanasoulis is in the nature of debt or equity.

c. Any claim for damages that the LPs may assert against Ms. Athanasoulis.

d. The Arbitration will not consider any claims between Ms. Athanasoulis and Cresford Capital/Dan Casey.

e. The LPs will reserve their rights with respect to whether Mr. Horton's decision at phase 1 of the Arbitration regarding enforceability is rendered *res judicata*.

f. At the conclusion of the Arbitration the Proposal Trustee will make a determination as to whether Ms. Athanasoulis' claim is provable, will value it and determine its priority.

g. The parties' rights to appeal are preserved under the *BIA*.

The court directed counsel to return for a further case conference on July 29, 2022.

[22] On July 4, 2022 the Sponsor advised that it would be withdrawing funding from the Proposal Trustee. It objected to funding the estimated $1.485 million in additional funding that the Proposal Trustee and indicated would be needed by it and its external counsel to complete the administration of these proceedings.[3]

[23] By the July 29, 2022 case conference, the Sponsor had been provided with a copy of the Arbitration Award and the Agreement to Arbitrate. The parties continued to have differing views on whether the Proposal Sponsor was obligated to fund the Proposal Trustee's fees and expenses for phase 2 of the Arbitration. Accordingly, the Proposal Trustee's funding motion was scheduled.

[24] Although no formal stay was ordered, phase 2 of the Arbitration has not been rescheduled, pending the outcome of this motion, since the Proposal Trustee requires funds to participate in it. The Proposal Trustee and Ms. Athanasoulis anticipate that the phase 2 proceeding contemplated by the Agreement to Arbitrate will require additional fact and expert evidence. The original schedule had set aside two weeks in September, 2022 for phase 2 of the Arbitration, before any consideration of including the LPs' claims.

[25] In the intervening timeframe, the Proposal Trustee and Ms. Athanasoulis did attend a mediation to try to come to a resolution of the Athanasoulis Claim, but that mediation was not successful.

[3] This estimate assumed that the three remaining disputed claims would be adjudicated in the manner indicated by the Proposal Trustee, with no further procedural motions. Also included in this budget were estimated Administrative Fees and Expenses associated with the phase 2 of the Arbitration. The amount for this portion of the future fees was initially estimated to be approximately $500,000, but that estimate is now approximately $700,000. However, other disputed claims have been resolved such that the overall estimate for future funding that the Proposal Trustee anticipates remains at an estimated $1.485 million.

[26] On October 13, 2022, shortly before the return of this funding motion, the LPs provided a draft notice of motion indicating their intention to bring a motion for declarations that: (a) any claim by Ms. Athanasoulis to the proceeds of the YSL Project under any profit-sharing arrangement is subordinate to their entitlement to such proceeds; and (b) Ms. Athanasoulis' profit-sharing claim is unenforceable against the Debtors. The LPs' assertions are based primarily on alleged representations and promises made to them by Ms. Athanasoulis.

[27] The Proposal Trustee's Notice of Motion on this motion seeks an order declaring that:

a. The Proposal Trustee's Administrative Fees and Expenses have been reasonably incurred.

b. The Sponsor remains bound by the Proposal.

c. The Sponsor is required to fund the Administrative Fees and Expenses of the Proposal Trustee pursuant to the Proposal.

d. The commencement and continuation of Arbitration to determine the Athanasoulis Claim was a valid exercise of the Proposal Trustee's power under the Proposal or the *BIA*.

[28] The Sponsor does not dispute that it remains bound by the Proposal to fund Administrative Fees and Expenses reasonably incurred. It disagrees on whether the Proposal requires it to fund the Proposal Trustee's fees and expenses that will be incurred in respect of phase 2 of the Arbitration.

[29] The court does not technically need to deal with the Proposal Trustee's request for a declaration that its Administrative Fees and Expenses have been reasonably incurred up until now. The Sponsor is no longer seeking to claw-back prior expenses that the Proposal Trustee has already been paid from the initial funding reserve. This includes fees and expenses associated with phase 1 of the Arbitration.

[30] During the hearing, and considering the most up to date positions, the Proposal Trustee re-stated the issues to be decided on this motion:

a. Whether the commencement and continuation of Arbitration to determine the Athanasoulis Claim was a valid exercise of the authority granted to the Proposal Trustee under the Proposal or the *BIA* (the "Jurisdiction Question" below), and therefore are any Administrative Fees and Expenses associated with it reasonably incurred?

b. If not, and in the alternative, is the question of whether the Sponsor is obligated to fund the Administrative Fees and Expenses of the Proposal Trustee and its counsel associated with phase 2 of the Arbitration *res judicata* and has this court already ruled that phase 2 of the Arbitration should proceed in some fashion, either with or without the added issues raised by the LPs?

c. Should there be any other order made at this time regarding the approval of the fees of the Proposal Trustee and its counsel?

d. Should the Sponsor pay the Proposal Trustee's costs of this motion, which are rolled up in its defence of the reasonableness and appropriateness of the Arbitration process?

Analysis

The Positions of the Parties

[31] The focus of the analysis is on the question of whether any Administrative Fees and Expenses associated with completing phase 2 of the Arbitration would be "reasonably incurred," such that the Sponsor is obligated to indemnify the Proposal Trustee for them under s. 11.01 of the Proposal.

[32] The Sponsor argues that the Proposal Trustee should have either allowed or disallowed the Athanasoulis Claim without resorting to arbitration. The Sponsor says the Proposal Trustee should determine and value that claim on its own, with such input from Ms. Athanasoulis and others as it deems appropriate. This process, the Sponsor postulates, could be completed more efficiently and at a significantly lesser cost than through the Arbitration.

[33] The Proposal Trustee argues that, even with the benefit of hindsight, a process outside of the Arbitration resulting in an allowance or disallowance of the Athanasoulis Claim would not necessarily have been more cost effective or timely. It postulates that both parties would have inevitably challenged the Proposal Trustee's decision regarding the determination of the Athanasoulis Claim under s. 37 of the *BIA*. Either Ms. Athanasoulis would appeal a decision against her to the court, or the LPs would further challenge a ruling that favoured Ms. Athanasoulis. The Proposal Trustee believes that these appeals or challenges to the court under s. 37 of the *BIA* would have the potential to involve the same evidentiary input, time and expense as the Arbitration.

[34] The Proposal Trustee likens the Arbitration to the appointment of a claims officer to adjudicate the Athanasoulis Claim and urges the court to permit that process to now run its course through phase 2 of the Arbitration.

[35] The Proposal Trustee also maintains that it was reasonable to have entered into the Agreement to Arbitrate and that it cannot now renege and disallow the Athanasoulis Claim simply because the Sponsor does not like the outcome of phase 1. The Sponsor counters that if the Agreement to Arbitrate, the terms of which it only had full disclosure of in July 2022, improperly delegates to the Arbitrator the Proposal Trustee's responsibility for determining and valuing the Athanasoulis Claim and was entered into without authorization or jurisdiction, then it is invalid *ab initio* and unenforceable.

[36] Ms. Athanasoulis supports the Proposal Trustee's position and adds that she is an innocent third party. Having contracted with the Proposal Trustee for an arbitration in two phases and having herself invested significant time and expense on phase 1, it would be unfair to her to now return to square one for the determination and valuation of her claim.

[37] Ms. Athanasoulis further argues that there is no principled distinction between the jurisdiction to arbitrate phase 1 vs. phase 2 of the Arbitration. She contends that the Sponsor's withdrawal of its objection to paying the fees and expenses for phase 1 is a concession that arbitrating in phase 1 was authorized and within the jurisdiction of the Proposal Trustee, and thus phase 2 must be as well.

[38] The LPs still intend to argue that they are not bound by any findings in the Arbitration or its outcome, and that the Athanasoulis Claim is subordinate to theirs. Neither of those arguments are before the court now. However, should the court find that the Proposal Trustee lacked the authority or jurisdiction to arbitrate the Athanasoulis Claim, that would make their intended motion less complicated and possibly moot, depending on the Proposal Trustee's timing and ultimate determination of the Athanasoulis Claim.

The Issues

A) The Jurisdiction Question

i) Contractual and Statutory Framework

[39] Section 3.02 of the Proposal provides that the Proposal Trustee will assess claims in accordance with s. 135 of the *BIA*.

[40] Section 135 of the *BIA* provides that:

> (1) The trustee shall examine every proof of claim or proof of security and the grounds therefor and may require further evidence in support of the claim or security.
>
> (1.1) The trustee shall determine whether any contingent claim or unliquidated claim is a provable claim, and, if a provable claim, the trustee shall value it, and the claim is thereafter, subject to this section, deemed a proved claim to the amount of its valuation.

ii) Relevant Jurisprudence Relied Upon by the Parties

[41] The Sponsor objects to providing additional funding for phase 2 of the Arbitration on the grounds that the Arbitration falls outside the Proposal Trustee's mandate under the Proposal, which is to determine and resolve disputed claims in accordance with s.135 of the *BIA*. The Sponsor maintains that because the Proposal Trustee improperly delegated that decision-making function to the Arbitrator and assumed the role of adversary, rather than the decision-maker, any Administrative Fees and Expenses associated with phase 2 of the Arbitration will not be reasonably incurred.

[42] The Sponsor relies upon the recent decision of this court *In the Matter of the Proposal to Creditors of Conforti Holdings Limited*, 2022 ONSC 3264, leave to appeal refused, 2022 ONCA 651. In *Conforti*, the court declined to relieve a trustee of its responsibility under s. 135 of the *BIA* to determine a particular claim through a single claims process under the supervision of the

Bankruptcy Court and declined to approve the trustee's suggestion that it be determined, instead, by a foreign court.

[43] This court held in *Conforti* that s. 135(1.1) of the *BIA* contains mandatory language that "unambiguously" requires the Proposal Trustee itself to determine and value claims. *Conforti* confirms, at para. 42, that:

> The regime under the *BIA* provides for a summary procedure for (i) determination by the trustee of whether a contingent or unliquidated claim is a provable claim, and, if so, (ii) for the trustee to value it. [...] Insolvency proceedings under the *BIA* are subject to court supervision, and the court is able to give directions for the timely and efficient determination of claims.

[44] This is not the first time a trustee's "mandatory statutory duty to review claims and value unliquidated or contingent claims" has been recognized: see *Asian Concepts Franchising Corporation (Re)*, 2018 BCSC 1022, 62 C.B.R. (6th) 123, at para. 99.

[45] Unlike in *Conforti*, the Proposal Trustee says it is not seeking to dispense with any obligation to determine the Athanasoulis Claim. It says it still intends to go through the motions of that determination but wishes to do so with the benefit of the Arbitrator's decision in phases 1 and 2.

[46] The Proposal Trustee also seeks to distinguish *Conforti* on the grounds that it has a very broad discretion under s. 135 of the *BIA* to obtain or require further evidence in support of a claim and has the power under s. 30 to bring, institute or defend any action or legal proceeding relating to the property of the bankrupt and to compromise any claim made by or against the estate. The Proposal Trustee argues that this permits a trustee to arbitrate a claim; or, at the very least, that this permits the Proposal Trustee to use an arbitration process to assist in the development of the evidence and facts that will be needed to determine and value a claim.

[47] The Proposal Trustee defends the Arbitration process as fair, reasonable and transparent. It emphasizes the importance of its role in ensuring all stakeholder interests are protected (as was envisioned in *Asian Concepts*, at paras. 55-56, 98, for example). The Proposal Trustee's contends that its decision to gather facts in respect of the Athanasoulis Claim by way of Arbitration was a reasonable decision and that it was an appropriate process to achieve a fair determination of the merits of the Athanasoulis Claim because it tested the potentially relevant evidence. It maintains that there is no single correct way to value a claim and that a trustee's decision should be afforded deference: see *Galaxy Sports Inc. (Re)*, 2004 BCCA 284, 29 B.C.L.R. (4th) 362, at paras. 39-43.

iii) The Agreement to Arbitrate – is it Beyond the Scope of s. 135 of the *BIA*?

[48] In theory, the Proposal Trustee does have a broad discretion under s. 135 of the *BIA* that might justify its participation in adversarial proceedings that could inform the eventual determination of claims. The Proposal Trustee seeks to characterize what the Arbitrator was asked to do as a fact finding exercise: to determine whether Ms. Athanasoulis was an employee who was constructively dismissed and whether she had an oral profit sharing agreement. The issue here is

whether the Agreement to Arbitrate in this case—which was not before the court and had not been disclosed to the Sponsor or the LPs until sometime in July, 2022—went beyond a fact finding exercise.

[49] Although no determination need be made on this point, the Proposal Trustee's participation in phase 1 of the Arbitration may have been sound in the sense that the necessary parties and information were before the Arbitrator to enable him to make determinations about the existence of the oral profit sharing agreement and a finding of constructive dismissal. The Proposal Trustee can consider and take into account these inputs from the Arbitration in its determination and valuation of the Athanasoulis Claim.

[50] Since the Sponsor is no longer challenging the right of the Proposal Trustee to be indemnified for the Administrative Fees and Expenses incurred in respect of phase 1 of the Arbitration, the issue now before the court is whether the Proposal Trustee is acting within the scope of s. 135 of the *BIA* by engaging in phase 2 of the Arbitration to determine whether to allow the Athanasoulis Claim, and if so in what amount.

[51] The Proposal Trustee concedes that the Arbitrator's determination of the damages question in phase 2 of the Arbitration would be both informative and probative, and that the Proposal Trustee's determination of the Athanasoulis Claim would be heavily influenced by the Arbitrator's decision. The suggestion that the Proposal Trustee could, after the Arbitration, still determine and value the Athanasoulis Claim in a manner inconsistent with the decision of the Arbitrator on liability and damages is difficult to reconcile with the words of the Agreement to Arbitrate and the intended binding nature of arbitrations under s. 37 of the *Arbitration Act 1991*, S.O. 1991, c. 17.

[52] I find that phase 2 of the Agreement to Arbitrate goes beyond a fact finding exercise. By its very terms, the Agreement to Arbitrate contemplates an eventual ruling from the Arbitrator on "damages" (the quantum of the Debtors' liability) at the end of phase 2. On their face, the terms of the Agreement to Arbitrate contemplate a final adjudication by the Arbitrator. That amounts to an improper delegation to the Arbitrator by the Proposal Trustee of its ultimate responsibility to determine and value the Athanasoulis Claim.

[53] It was suggested that the court would be effectively ordering, or approving, the Proposal Trustee to breach the Agreement to Arbitrate if the Sponsor's position with respect to the funding of phase 2 of the Arbitration is accepted. I do not see it that way. If the Proposal Trustee did not have the authority to agree to phase 2 of the Arbitration as was provided for in the Agreement to Arbitrate because it amounted to an improper delegation of its responsibility to the Arbitrator, then that aspect of the Agreement to Arbitrate is unenforceable as against the Proposal Trustee. Further, as a practical matter, if the Sponsor is not required to fund the Administrative Fees and Expenses associated with phase 2 of the Arbitration, it cannot proceed.

[54] I also do not accept the assertion that just because the Sponsor is no longer challenging its obligation to fund the Proposal Trustee's Administrative Fees and Expenses incurred in connection with phase 1 of the Arbitration, that the court is bound to accept that entering into the Agreement to Arbitrate was a valid exercise of the Proposal Trustee's discretion and a valid delegation of its responsibility to the Arbitrator in all respects, or that the Sponsor is estopped from asserting that

any aspect of the Agreement to Arbitrate exceeded the Proposal Trustee's authority under s. 135 of the *BIA*.

iv) Would the Cost of this Arbitration be a Reasonably Incurred Expense?

[55] One of the other grounds upon which the Sponsor argued that the anticipated Administrative Fees and Expenses for phase 2 of the Arbitration would not be reasonably incurred was because they would be the product of a complex, lengthy and expensive process that is not in keeping with the summary and efficient adjudication of claims envisioned by the *BIA*, especially one that might not have resulted in a final resolution of the Athanasoulis Claim without the willing participation of the LPs,[4] leaving the LPs' priorities and other enforceability issues to be determined through some other process.

[56] Section 135 of the *BIA* is intended to be a summary procedure for the determination of claims, animated by the objectives of speed, economy and informality: see *Conforti*, at para. 43 and *Asian Concepts*, at para. 53.

[57] The decision on the Jurisdiction Question renders it unnecessary to decide whether the anticipated budgeted cost of phase 2 of the Arbitration represents anticipated reasonably incurred Administrative Fees and Expenses that the Sponsor should be required to fund. The court will not order the Sponsor to fund this aspect of the Arbitration that involves the ultimate determination of this claim by someone other than the Proposal Trustee as that would not be a determination of the Athanasoulis Claim in accordance with s. 135 of the *BIA*.

v) Section 135 *BIA* Determination of the Athanasoulis Claim

[58] The Proposal Trustee has identified various aspects of what had been expected to be resolved through the anticipated phase 2 Arbitration that will still require factual inputs and findings for the Proposal Trustee to make its determination of the Athanasoulis Claim. For example, to determine the meaning of "profits" under the oral profit sharing agreement, and when and how they should be calculated, expert valuation evidence may be required. This was part of the justification for the Arbitration process envisioned, and has not been resolved by the court's finding that the process agreed to went too far by improperly delegating the ultimate issue to be decided by the Proposal Trustee to the Arbitrator.

[59] Further, whether the Athanasoulis Claim is a provable claim under s. 135 of the *BIA* depends on whether the claim is in debt or equity, which in turn may require further evidence and inputs from other stakeholders, like the LPs. Not only would the LPs potentially have relevant information, but they also have a direct interest in these determinations.

[60] The Proposal Trustee has the power under s. 135 of the *BIA* to seek additional information and documents from the claimant: see *Urbancorp Cumberland 2 GP Inc.*, 2022 ONSC 2430, at

[4] As previously indicated, there is a dispute about whether the LPs agreed to arbitrate their priority and enforceability challenges to the Athanasoulis Claim. The court was not asked to determine whether the LPs had in fact agreed to arbitrate their issues in the expanded phase 2 of the Arbitration. I do not need to decide this question to decide the funding motion.

paras. 23, 26. It remains open to the Proposal Trustee under s. 135 of the *BIA* to receive and consider expert input from Ms. Athanasoulis and other stakeholders.

[61] The broad discretion afforded to the Proposal Trustee also allows it to seek out its own expert input, as well as information and input from the LPs and other stakeholders in respect of the issues it must decide.

[62] In these circumstances, the Proposal Trustee will need to carry out its responsibilities under s. 135 of the *BIA*, get the factual and other inputs it requires from witnesses, other stakeholders, experts and the like and determine whether the Athanasoulis Claim has been proven and, if so, at what amount it should be valued.

[63] The Proposal Trustee complains that the Sponsor has not spelled out an alternative process to the Arbitration for doing this.

[64] In the absence of any proposed alternative, the Proposal Trustee is entirely unencumbered and may determine its own process for how it wishes to do this, which will be afforded significant deference. According to the Court of Appeal in *Galaxy*, at paras. 39 and 44,

a. the Proposal Trustee is entitled to evaluate the Athanasoulis Claim in accordance with s. 135(1.1) with significant discretion, taking into account factors that may appear in the *BIA*;

b. there is no one "correct" answer to the valuation of the Athanasoulis Claim;

c. the Proposal Trustee's valuation of the Athanasoulis Claim will be scrutinized on a "reasonableness" standard; and

d. the Proposal Trustee can use its knowledge and expertise to consider whether, as a factual matter, the valuation as to the full amount of the Athanasoulis Claim is appropriate.

[65] The Proposal Trustee is concerned that this may lead to *de novo* appeals or challenges (by either Ms. Athanasoulis or the LPs) and could end up being as much or more expensive than the anticipated cost of phase 2 of the Arbitration. There is no crystal ball that can foretell this.

[66] The Sponsor says that it will not micromanage this aspect of the Proposal Trustee's determination of the Athanasoulis Claim. While the Sponsor does not expect that this alternative process will end up costing as much as the current estimate for phase 2 of the Arbitration, it is prepared to accept the possibility that it does. The Sponsor has said it will pay for the Proposal Trustee to develop and follow a process to determine and value the Athanasoulis Claim in accordance with s. 135 of the *BIA*.

[67] The Proposal Trustee must determine how to reasonably determine and value the Athanasoulis Claim in a timely and principled manner. It will be afforded significant deference. All parties agree that it can use the Arbitration Award from phase 1 of the Arbitration and build

on it so that time and effort is not wasted. The goal is not the gold standard of coming up with a process that cannot be challenged.

[68] The Proposal Trustee may choose to invite expert evidence and inputs from Ms. Athanasoulis and then determine if it needs its own expert to review and comment upon what is provided. It may choose to share that plan with the other stakeholders participating in this motion and seek their input. If it chooses to share its plan with the Sponsor and/or other stakeholders, and if the parties require some further direction and assistance from the court, they may arrange a case conference before me.

[69] In any event, the parties will eventually need to come back on a scheduling appointment to determine the sequencing and timing of the LPs' priorities and enforceability motion, but only after that motion (with supporting evidence) has been served and the parties have met and conferred amongst themselves to consider the appropriate timing and sequencing of all that needs to occur.

[70] Whatever process the Proposal Trustee may adopt, the Sponsor remains obligated under the Proposal to indemnify the Proposal Trustee for the Administrative Fees and Expenses reasonably incurred going forward to the final determination of the Athanasoulis Claim.

B) The *Res Judicata* and Estoppel Argument(s)

i) Res Judicata

[71] There can be no finding of *res judicata* with respect to the issues raised on this funding motion regarding the Sponsor's obligation to fund phase 2 of the Arbitration.

[72] The Proposal Trustee and Ms. Athanasoulis argue that Gilmore J. held, at two separate case conferences in May and June 2022, that arbitration was an appropriate way to proceed, and that issue estoppel prevents the court from revisiting this in the context of this funding motion. I disagree.

[73] There are three requirements for invoking issue estoppel: (i) the same question has or could have been decided in a prior proceeding; (ii) the decision giving rise to estoppel is final; and (iii) the parties to the decision giving rise to estoppel are the same as the parties to the subsequent proceeding in which estoppel is claimed: see *The Catalyst Capital Group Inc. v. VimpelCom Ltd.*, 2019 ONCA 354, 145 O.R. (3d) 759, at para. 25. It is the first requirement upon which the *res judicata* argument fails in this case.

[74] The Proposal Trustee argues that the endorsement of Gilmore J. arising out of the June 8, 2022 case conference requires an arbitration of the Athanasoulis Claim because it was stated in the endorsement that the "arbitration must prevail" and the Sponsor never sought to appeal that declaration.

[75] I do not read the June 8, 2022 endorsement as ordering an arbitration. Rather, it was the court's strong preference that the parties agree to expand the Arbitration to address the issues raised by the LPs and avoid a parallel, costly and time consuming motion process to determine the priority

and enforceability issues. I am not aware of any authority upon which the court can order unwilling parties to arbitrate a dispute; that is a matter of private agreement. The court was simply strongly encouraging the parties to make such an agreement, building upon the arbitration process already in place.

[76] Nor do I agree with the implicit suggestion that the same question about the authority of the Proposal Trustee to enter into the Agreement to Arbitrate and to delegate its responsibility for determining and valuing the Athanasoulis Claim to the Arbitrator has been or could have been previously decided by Gilmore J. at the earlier case conferences. Leaving aside the nature of those case conferences and the typical procedural scope of directions from the court, it is clear that is not what Gilmore J. understood to be happening. To the contrary, her June 8, 2022 endorsement records that:

> At the conclusion of the arbitration the Proposal Trustee will make a determination as to whether Ms. Anathasoulis' [*sic*] claim is provable and will value it and determine its priority.

[77] At that time, the court did not have the Agreement to Arbitrate with the full description of the issues being submitted to arbitration and cannot be taken to have made any meaningful assessment as to whether the statement that there was still something left for the Proposal Trustee to determine at the end of the Arbitration was a fair characterization of what had been agreed to. The court did not previously order the parties to arbitrate, nor did it make any finding that phase 2 of the Arbitration could be conducted in a manner consistent with s. 135 of the *BIA*. There is no *res judicata*.

ii) Other Estoppel Considerations

[78] That said, it was prudent of the Sponsor to drop its opposition to the Proposal Trustee's request for approval of the expenses associated with phase 1 of the Arbitration, already incurred and paid. Regardless of the court's determination of the threshold Jurisdiction Question in relation specifically and only to phase 2 of the Arbitration, the Sponsor would have faced other obstacles in attempting to claw back from the Proposal Trustee Administrative Fees and Expenses incurred and paid for out of the initial reserve, including for phase 1 of the Arbitration.

[79] These obstacles would include the Sponsor's inaction and failure to ask any questions or raise any complaint about, or object to phase 1 of the Arbitration proceeding while it was ongoing. However, the Sponsor's concession obviates the need for any ruling on this.

iii) The Timing of Objections and Related Considerations

[80] Ms. Athanasoulis is understandably concerned about having engaged in phase 1 of a two phase arbitration process in good faith and now facing objections to the jurisdiction or authority of the Proposal Trustee to have entered into the Agreement to Arbitrate.

[81] Unfortunately, the Sponsor and the LPs did not have a copy of the Agreement to Arbitrate until July, 2022. Their concerns were raised in a timely manner upon learning more about the scope of the Arbitration and its anticipated cost. The fact that this discovery also coincided with

their learning that the phase 1 outcome favoured Ms. Athanasoulis does not automatically lead to the inference that their objections are disingenuous.

[82] In any event, no one is suggesting that the work done in phase 1 of the Arbitration is lost. It will be one of the inputs that the Proposal Trustee will use to determine and value the Athanasoulis Claim. All parties agree on this.

[83] While I do not go so far as to accept the suggestion by the Sponsor and LPs that Ms. Athanasoulis knowingly took on the risk of this challenge and outcome, the Sponsor and LPs were left out of the process and cannot be precluded from raising the legal objections that have ultimately dictated the outcome of this motion on the Jurisdiction Question, as it relates to phase 2 of the Arbitration.

C) Fee Approvals

[84] Gilmore J.'s endorsement scheduled this funding motion to determine the Proposal Trustee's entitlement to be indemnified for the costs of the Arbitration. The indemnity reimbursements taken up until now from the reserve fund are no longer at issue. The relief sought by the Proposal Trustee for the approval of its past activities and fees might have been warranted if the challenge to entitlement to indemnification for expenses incurred in phase 1 of the Arbitration was still at issue.

[85] However, this is no longer at issue. There is no immediate reason or need to attempt to deal with the broader requests for general approval of the activities and fees of the Proposal Trustee and its counsel.

[86] The Sponsor is right that, in general, such requests should be supported by fee affidavits: see *Jethwani v. Damji*, 2017 ONSC 1702, 46 C.B.R. (6th) 96, at paras. 8-11.

[87] For the same reason, it is also inappropriate to grant the requested charge over all past and future distributions to the Sponsor. This issue was not fully argued and I was not taken to the evidence or authority that I would need to consider to make such an order.

[88] Instead, the Proposal Trustee may now wish to prepare a new budget and request additional reserve funding for the indemnity obligations of the Sponsor. If the Sponsor does not agree to supplement the reserve, the parties can arrange to come back for a case conference for further consideration of the questions of up front funding and/or security for future funding to be provided by the Sponsor.

D) Costs

[89] Despite having found that the contemplated phase 2 of the Arbitration goes beyond the scope of what the Proposal Trustee was authorized to agree to, given the original position of the Sponsor that it was also challenging its obligation to fund expenses for phase 1 and given the added complications introduced by the LPs, I consider it to have been reasonable for the Proposal Trustee to have brought this motion for directions.

[90] The Proposal Trustee's and its counsel's costs of this motion were reasonably incurred as part of the administration of distributions and the resolution of unresolved claims such that those costs should be indemnified by the Sponsor under the s. 11.1 of the Proposal on the basis that they were reasonably incurred Administrative Fees and Expenses.

[91] Ms. Athanasoulis has asked to be awarded some reasonable costs thrown away in the event the Arbitration is not proceeding to phase 2. She spent $300,000 on phase 1 (in line with the Proposal Trustee's disclosed legal costs for phase 1) and had started working with her expert on phase 2. I understand that there was an agreement that each side would bear their own costs of the Arbitration.

[92] I agree that if Ms. Athanasoulis had actually incurred costs thrown away of the Arbitration, that are now wasted, she might be entitled to an award for her trouble: see *Caldwell v. Caldwell*, 2015 ONSC 7715, 70 R.F.L. (7th) 397, at paras. 10-12.

[93] However, given that the phase 1 Arbitration findings will be the factual predicate upon which the determination of her claim will proceed and that it is reasonable to expect that Ms. Athanasoulis will require expert input, regardless of the procedure, to have her claim determined by the Proposal Trustee, I am not convinced that she has suffered any costs thrown away.

[94] The parties are just now pivoting to a different process for the final determination of the Athanasoulis Claim, but the onus is still on her to prove it. It is difficult to see how she has wasted the cost of whatever work she did in furtherance of her quest to persuade the Arbitrator to decide in her favour the same issue that the Proposal Trustee will now take into consideration when determining her claim. All the work should be usable to support the proof of her claim to the Proposal Trustee.

[95] As such, no costs thrown away are awarded to Ms. Athanasoulis.

Final Disposition

[96] The court's decision on each of the issues on this funding motion, as re-stated by the Proposal Trustee, is as follows:

a. The continuation of phase 2 of the Arbitration provided for in the Agreement to Arbitrate the Athanasoulis Claim is not a valid exercise of the authority granted to the Proposal Trustee under the Proposal or s. 135 of the *BIA*. Therefore, the court makes no order requiring the Sponsor to fund (and/or indemnify the Proposal Trustee for) the budgeted Administrative Fees and Expenses associated with phase 2 of the Arbitration (of approximately $700,000).

b. The questions of whether phase 2 of the Arbitration was a procedure that the Proposal Trustee had the jurisdiction to engage in, and the Sponsor's obligation to fund the Administrative Fees and Expenses of the Proposal Trustee associated therewith, are not barred by *res judicata* or any other estoppel or laches.

c. The Sponsor is required to indemnify the Proposal Trustee for all of the reasonably incurred Administrative Fees and Expenses in relation to the determination and valuation of the Athanasoulis Claim, including for phase 1 of the Arbitration and for whatever procedure the Proposal Trustee, in its discretion, determines appropriate to receive the further evidence and positions of Ms. Athanasoulis and other interested stakeholders and any expert inputs deemed necessary.

d. The Proposal Trustee should first determine how it intends to proceed in light of the court's decision on this motion, and may prepare a budget for the anticipated Administrative Fees and Expenses associated with this exercise, or seek indemnification after the fact, as it deems appropriate.

e. If asked to do so and the Sponsor is not prepared to top up the reserve for the funding of the Proposal Trustee's anticipated Administrative Fees and Expenses to complete the determination and valuation of the Athanasoulis Claim, the parties may request a case conference before me so that the court can provide further directions in this regard and any related issues. The parties are directed to confer about these issues before scheduling a case conference so that the appropriate amount of court time is reserved.

f. If the LPs are proceeding with their proposed motion, they shall serve their motion record(s) with supporting evidence and, after that, the parties shall confer about the timetabling and sequencing of those motions and then seek a scheduling appointment (if all agree) or a longer case conference (if all do not agree) for directions, timetabling and a motion hearing date if determined appropriate.

g. There have been no costs demonstrated to have been thrown away as a result of the court's ruling on this motion, and none are awarded.

h. The costs of the Proposal Trustee and its counsel for this motion were reasonably incurred and may be paid out of the remaining reserve fund and/or a claim for reimbursement by the Sponsor for those costs may be made under the Proposal.

[97] This endorsement and the orders and directions contained in it shall have the immediate effect of a court order without the necessity of the formal issuance and entry of an order.

KIMMEL J.

Date: November 1, 2022

TAB 27

CITATION: YG Limited Partnership and YSL Residences (Re), 2021 ONSC 4178
COURT FILE NOS.: CV-21-00655373-00CL/BK-21-02734090-0031, CV-21-00661386-00CL & CV-21-00661530-00CL
DATE: 20210629

SUPERIOR COURT OF JUSTICE – ONTARIO
(COMMERCIAL LIST)

RE: IN THE MATTER OF THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, C. B-3, AS AMENDED

AND:

IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF YG LIMITED PARTNERSHIP AND YSL RESIDENCES

APPLICATION UNDER THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, C. B-3, AS AMENDED

AND RE: 2504670 CANADA INC., 8451761 CANADA INC. and CHI LONG INC., Applicants

AND

CRESFORD CAPITAL CORPORATION, YSL RESIDENCES INC, 9615334 CANADA INC., YG LIMITED PARTNERSHIP and DANIEL CASEY, Respondents

AND RE: 2583019 ONTARIO INCORPORATED AS GENERAL PARTNER OF YONGESL INVESTMENT LIMITED PARTNERSHIP, 2124093 ONTARIO INC., SIXONE INVESTMENT LTD., E&B INVESTMENT CORPORATION and TAIHE INTERNATIONAL GROUP INC., Applicants

AND

9615334 CANADA INC. AS GENERAL PARTNER OF YG LIMITED PARTNERSHIP and YSL RESIDENCES INC., Respondents

BEFORE: S.F. Dunphy J.

COUNSEL: *Harry Fogul* and *Miranda Spence*, for YG Limited Partnership and YSL Residences Inc.

Shaun Laubman and *Sapna Thakker*, for 2504670 Canada Inc., 8451761 Canada Inc., and Chi Long Inc.

Alexander Soutter, for YongeSL Investment Limited Partnership, 2124093 Ontario Inc., SixOne Investment Ltd., E&B Investment Corporation, and TaiHe International Group Inc.

David Gruber, Jesse Mighton, and *Benjamin Reedijk,* for Concord Properties Developments Corp. and its affiliates

Jane Dietrich and *Michael Wunder,* for 2292912 Ontario Inc. and Timbercreek Mortgage Servicing Inc.

Robin B. Schwill, for KSV Restructuring Inc. in its capacity as the proposal trustee

Roger Gillot and *Justin Kanji,* for Kohn Pedersen Fox Associates PC

Reuben S. Botnick, for Royal Excavating & Grading Limited COB as Michael Bros. Excavation

Daniel Naymark and *Jamie Gibson*, for Sarven Cicekian, Mike Catsiliras, Ryan Millar and Marco Mancuso

Brendan Bowles and *John Paul Ventrella*, for GFL Infrastructure Group Inc.

Mark Dunn and *Carlie Fox*, for Maria Athanasoulis

George Benchetrit, for 2576725 Ontario Inc.

Joshua B. Sugar, for R. Avis Surveying Inc.

Paul Conrod, for Restoration Hardware Inc.

James MacLellan and *Jonathan Rosenstein,* for Westmount Guarantee Services Inc.

Albert Engle, for Priestly Demolition Inc.

HEARD at Toronto: June 23, 2021

AMENDED REASONS FOR INTERIM DECISION

Note: these reasons were amended on July 2, 2021 as more fully described in the in the concluding paragraphs hereof.

[1] The debtors are seeking approval of a bankruptcy proposal that has obtained the near unanimous approval of those affected creditors who cast a vote. Two groups of limited partnership unitholders have challenged the actions of the General Partner of the debtor YG Limited Partnership for much of the past year and urge me to annul the bankruptcy entirely or to reject the proposal and, if need be, to allow a Receiver or Trustee in bankruptcy to canvass the market fairly and objectively. Another unsecured creditor urges me to disregard much of the appraisal evidence tendered because she has been excluded from examining it and the result is a record that casts grave doubt as to whether fair value for stakeholders is being realized by this process.

[2] For the reasons that follow, I have decided that I will not approve the Proposal in the form it has been presented to me. The Proposal is yet able to be amended pursuant to art. 3.01 thereof and it is possible that an amendment may be formulated to address the concerns raised by the findings I outline below before a final decision on the fate of the Proposal is made.

Background facts

[3] A central issue in this case is the value of the "YSL Project" – the property owned by the debtor YSL as bare trustee for the limited partnership (the debtor YG LP) charged with developing it. Valuation is an area on which I must tread lightly in terms of what I can record in writing so as not to impact adversely any potential sale process that may be necessary in future.

[4] What follows is a general description of the capital structure of the debtors and the project sufficient to permit an understanding of the issues. For comparison purposes, it is relevant to consider the size of the project. There is no dispute that the "as if completed" value of the project is above $1 billion. How much above and based on which assumptions is an issue, but I provide the round figure solely for comparison purposes relative to the debt and equity interests discussed.

[5] The project is fully zoned and permitted for construction of an 85-story retail and condominium complex planned for the corner of Yonge St. and Gerard in downtown Toronto. Substantial pre-sales have been made. Demolition of the old structures and shoring up of the excavation have been largely completed. Unfortunately, things ground to halt in March of 2020 and the project has been stuck in the "hole in the ground" stage ever since.

The project ownership structure

[6] YP GP has a General Partner with nominal capital and a nominal interest in the limited partnership. The "equity" in the partnership effectively resides in the "A" units with approximately $14.8 million in capital but a capped right to return on that capital equivalent

to interest (12.25% per year rate of return) and the “B” units who alone receive all of the residual profits from the project without limit.

[7] The owner of the “B” units and the General Partner are under common control within the Cresford group of companies as are the parties recorded as payees of the $38.3 million related party debt to which I shall refer.

The project debt structure

[8] The secured debt – including registered mortgages and construction liens – stands at about $160 million. The figure for secured debt is slightly misleading. There is just over $100 million in deposits from condominium pre-sales made for the most part prior to 2019. These are insured by the second secured creditor whose claim would increase dollar for dollar if the relevant purchase agreements were repudiated and the deposits had to be returned. For this reason and to have an “apples to apples” idea of the debt structure, a figure of about $260 million in secured debt is appropriate.

[9] The third-party unsecured debt that has been identified by the Trustee is in the range of approximately $20 million plus or minus a few million dollars depending upon reserves allowed for claims yet to be filed or finalized. There are also various litigation claims outstanding the largest of which is from a former officer claiming that the limited partnership was a common employer and seeking, among other things, to enforce oral profit-sharing agreements. I have reviewed the Trustee’s report and in particular the Trustee’s reasoned conclusion that these claims are too contingent to be considered valid for voting purposes. I concur in that assessment. A conservative and prudent assessment of potential total unsecured claims is thus in the range of about $25 million – a figure advanced with full knowledge that the total of all contingent claims identified could be in the same order of magnitude again. For the purposes of this motion, I find the figures estimated by me above are reasonable – those findings are, of course, without prejudice to the creditors holding such claims proving them in due course.

[10] There is also $38.3 million in outstanding advances to YG LP recorded on its books from related parties. I have found those claims to be equity claims for all purposes relevant to this hearing for reasons I shall expand upon below.

[11] In round figures, one can thus consider there to be approximately $260 million of secured debt and about $20-$25 million of unsecured debt outstanding. The Proposal assumes all of the former and would pay 58% of the latter when finalized. The “fulcrum” stakeholders in this case are thus the unsecured creditors to the extent of the 42% of their claims that are compromised ($8.4 to $10.5 million) plus the “A” limited partners in YG LP ($14.8 million plus accrued “interest” entitlements) – such figures based upon the estimates and rulings that I have made and explained herein.

Summary of nine findings made

[12] The process of sifting through the mountains of evidence presented to me by the parties has been made exceptionally time-consuming and tedious by reason of the lack of usable electronic indexing in much of the materials filed. Tabs or electronic hyperlinks within compilations of electronically filed documents are non-existent in all but the most recently filed documents and there are many, many thousands of pages of documents presented. The profession is going to need to get on top of this problem as judges cannot and will not in future undertake such gargantuan efforts to sift through a case when a few moments of care and attention at the front end could simplify it to such a great degree.

[13] Time does not permit me to set forth in writing a complete account of my review of the evidence and my conclusions – a written summary of which I was about 75% through before the impossibility of completing it in the form intended within the time available became obvious. I shall instead present below nine conclusions which encapsulate my reasons for finding that the Proposal as it currently stands has failed to satisfy me of the matters required by s. 59(2) of the BIA or the common law test of good faith.

(i) The McCracken Affidavit is inadmissible

[14] As is often the case in Commercial Court matters, this case proceeded on a "real time" schedule. In addition to the bankruptcy case that was commenced with an NOI filed on behalf of the debtors on April 30, 2021, there were two applications commenced the day before by two groups of YG LP limited partners seeking, among other things, the removal of the General Partner and various declarations challenging the authority of the General Partner to act on behalf of the partnership in any capacity and alleging breaches of fiduciary duty by the General Partner. The Proposal itself was filed on May 27, 2021 working towards a scheduled June 10, 2021 creditor meeting. On June 1, 2021 I issued directions for the conduct of all three proceedings with a view to having the sanction hearing ready to proceed on June 23, 2021.

[15] The Proposal Sponsor is Concord Properties. Concord is not a party to any of these proceedings although it is central to all three. Concord sponsored the Proposal and is bearing all the costs of it under a Proposal Sponsor Agreement dated April 30, 2021.

[16] The limited partner applicants issued subpoenas to Mr. McCracken – apparently the officer of Concord responsible for this Proposal. On the advice of counsel, Mr. McCracken declined to appear absent an order compelling him to do so. Counsel took the position that leave was required under the Bankruptcy Rules to compel him to appear in the bankruptcy proceeding and declined to produce him.

[17] The position taken was a curious one given my specific direction on June 1 that I was *not* applying the BIA stay to the two applications and that specific aspects of both

applications would be heard and decided together on June 23, 2021 when the fairness hearing was conducted. The case timetable made specific allowances for responding records with respect to the limited partner applications and facta in relation to them. My ruling on June 1, 2021 was in both the civil and bankruptcy proceedings and bore the style of cause of both.

[18] Whether leave was or was not formally required to *compel* Mr. McCracken to appear, his failure has consequences in terms of the fairness of the process leading to the approval motion in front of me. The opponents of the Proposal were deprived of the opportunity to explore aspects of the unfairness or unreasonableness of the Proposal that they had raised. There was insufficient time available in the tight timetable to drop everything and bring a leave application. The position taken ran utterly contrary to the spirit and intent of my ruling on June 1, 2021 at which Concord's counsel appeared *and made submissions*. This is the sort of issue that counsel applying the "three C's" of the Commercial List ought to have agreed to disagree upon and produced the witness without prejudice to objections that might be raised.

[19] It is against the foregoing backdrop that the affidavit of Mr. McCracken – delivered the day prior to the fairness hearing – must be considered.

[20] The affidavit was filed far too late to permit any interested party to respond to it effectively or to cross-examine upon it. None of the subject-matter of the affidavit was new information. The affidavit was entirely devoted to providing responses to various issues seen in written arguments or that arose on the cross-examination of other witnesses.

[21] Concord appeared to consider itself sufficiently at interest to appear through counsel on June 1, 2021 while declining to submit to examination because of its non-party status when preparations for this hearing were in full swing a few days later. Permitting the admission of this affidavit at this juncture would be to sanction unfairness of the highest order. A timetable was worked out for the hearing of this motion – worked out, I might add, at a motion that Concord was present at through counsel. Whether or not Concord had the *right* to insist upon a further motion to compel its attendance during the pre-hearing procedures, it certainly knew that taking that position when there was no time available to challenge it in court would have the practical effect that it did.

[22] Lying in the weeds is a strategy, but it does not confer the right to spring out of them at will. I find the McCracken affidavit to be inadmissible and attach no weight to it.

(ii) No weight can be attached to the CBR April 2021 Appraisal

[23] The parties have very hotly debated the valuation evidence that is on the record before me. A portion of that valuation evidence has been sealed. My reason for doing so is straightforward: the approval of the Proposal cannot be taken for granted and it is thus

reasonably foreseeable that the project may have to be sold by a Trustee or Receiver in the near future and the ability of whichever court officer is charged with undertaking that sale to achieve the highest and best price available ought not to be impaired more than the circumstances already have by the disclosure of appraisals that may serve to skew market expectations. A significant portion of such evidence is part of the public record and between the public information and the use of carefully-framed circumlocutions I believe that I can convey my conclusions and reasons for them regarding the valuation evidence with reasonable clarity.

[24] Two of the appraisals before me, both from CBRE, are the most central to the questions I must determine. The first in time is dated August 8, 2019 providing CBRE's opinion of value as at July 30, 2019. This appraisal was prepared for the parent company of the debtors within the Cresford group and is based on the particular assumptions set out therein, including some supplied by Cresford. The second in time, also by CBRE, is dated April 30, 2021 as of March 16, 2021. This latter appraisal was prepared for Concord based on the assumptions set out therein, including some supplied by Concord. I shall not discuss in a public document the actual appraisal amounts in either, focusing instead on the differences between them.

[25] For present purposes, it is sufficient for me to observe that the 2021 CBRE appraisal is lower than the 2019 CBRE appraisal and lower by an amount that is significantly higher than the sum of the compromised amount of unsecured claims under the Proposal plus the total capital of the "B" unitholders in YG LP.

[26] I find that I can attach little weight to the 2021 CBRE appraisal in these circumstances because:

a. The assumptions given to CBRE by Concord were materially different than those used in the 2019 CBRE appraisal including as to such things as leasable square footage of residential and retail space;

b. When it formulated the instructions to CBRE, Concord was in the process of attempting to negotiate a Proposal to acquire the property through the bankruptcy process given lack of limited partner consents and was being commissioned at a time when Concord had a clear and obvious interest in having appraisal evidence suggesting that the project was at least partly underwater;

c. The downward alterations made by Concord to the square footage assumptions used by CBRE are unexplained, untested and appear to be admitted as having been quite preliminary at all events;

d. Concord did not submit Mr. McCracken to cross-examination to examine in depth the reasons for the significant negative difference between the two instructions given to CBRE on the conflicting appraisals;

e. The differences between the two have not been reasonably or adequately reconciled. There has been no general downward correction to residential real estate in Toronto that has been brought to the court's attention nor can the difference between the two appraisals reasonably be attributed solely to pandemic-induced alterations to the retail environment.

(iii) ALL Construction Lien Claims are Unaffected Creditors under the Proposal

[27] Under the Proposal, Construction Lien Claims are defined as "Unaffected Creditors". The Trustee indicates that the total amount of such claims is $11.865 million. Of this total, fifteen lien claimants with $9.19 million in lien claims outstanding entered into assignment agreements with the Proposal Sponsor. As these are non-voting Unaffected Creditors under the Proposal, Concord required them to file claims as Affected Creditors in order to acquire the right to vote and to name a proxy designated by Concord.

[28] There was some controversy about what precisely the lien claimants received in return for agreeing to convert claims that were to be paid $1.00 per $1.00 of valid claims under the Proposal into claims receiving no more than $0.58 per dollar of claim value. The Trustee-reported second-hand information from Concord denying any "side" deals does little to address this concern. Assurances as to the lack of a side deal do not serve the purpose of permitting a reasonable understanding of the main deal. None of them have been disclosed beyond a skeletal summary and Concord declined to permit a representative to be examined prior to the hearing.

[29] It is of course open to the Proposal Sponsor to make any proposal that satisfies the formal requirements of the BIA if the debtor is prepared to adopt it and submit it to the creditors and the creditors are willing to accept it with their eyes open. In this case however the Proposal Sponsor has induced $9.19 million of otherwise Unaffected Creditors to file claims as something they are not by definition (i.e. Affected Creditors) thereby effectively reducing the size of the cap from $65 million to $55.8 million and the maximum pool of funds available to the actual Affected Creditors described by the Proposal from $37.7 million to $32.4 million. These are material changes impacting all Affected Creditors that follow from arrangements made by the Proposal Sponsor outside the terms of the Proposal.

[30] The Proposal makes no provision for creditors "downshifting" their claims voluntarily. Lien claims are defined as "Unaffected Claims" and I see no basis for them to be accepted under the Proposal on any other basis particularly where doing so operates to the obvious detriment of the affected class members. This is not a case of a

secured creditor valuing its security and filing an unsecured claim for the shortfall. There are consequences to such a valuation exercise that are absent here.

[31] The “electing” lien claimants have little in common with the actual Affected Creditors who had no election to make. Despite having made the election, assuming there was any basis in the Proposal to make such an election (and it appears to me that there was not), such creditors retained their security intact. Pursuant to art. 9.01 of the Proposal, the Proposal would have “no effect upon Unsecured Creditors” which definition does not cease to apply to them by virtue of a make-shift “election” for which the Proposal makes no provision. They did not agree to surrender their security nor even to value it in the bankruptcy process. They agreed to sell their claims on whatever terms they chose to accept from the Proposal Sponsor secure in the knowledge that if, for any reason, the Proposal does not move forward, their security remains intact and unaffected.

[32] This is an element of unfairness in this that I find particularly disturbing. It is all the more disturbing when I am not at all persuaded that the unsecured creditors face the spectre of near certain annihilation in the event of a bankruptcy or receivership but face the very real prospect of additional and illegitimate dilution of their claim value were I to approve the Proposal as presented with the presence of lien claimants in the Affected Creditor pool.

(iv) The related party claims must be treated as equity

[33] A fundamental principle of the BIA is that equity claims are subordinate to debt claims. This principle is voiced in s. 60(1.7) of the BIA that provides quite simply that ”[n]o proposal that provides for the payment of an equity claim is to be approved by the court unless the proposal provides that all claims that are not equity claims are to be paid in full before the equity claim is to be paid”. Section 140.1 expresses a similar requirement in respect of dividends more generally. While there is some similarity behind the concept of “equity claims” in Canadian insolvency law and that of “equitable subordination” the two are separate and one and must not be confused with the other: *U.S. Steel Canada Inc. (Re)*, 2016 ONCA 662 (CanLII) at para. 101.

[34] The limited partner applicants submit that the intercompany advances appearing in the general ledger of YG LP should be treated as equity claims within the meaning of the BIA. The debtors on the other hand urge me to pass over this issue entirely arguing that approval of the proposal does not entail approval of any payment of intercompany claims. Such claims will ultimately be determined by the Trustee and if disallowed for any reason will receive no distribution.

[35] I cannot accept the debtors’ argument that I should sweep the equity claims under the carpet to be dealt with another day in another forum. This is so for the following reasons:

a. The applicant limited partners have no standing to challenge the proof of the related party claims within the bankruptcy process even if their claims against related parties are not themselves released by the Proposal.

b. On June 1, 2021 I directed that issues raised in the two applications would be dealt with on June 23. A theme in those applications was, among others, the allegation that the General Partner had been seeking to divert substantial payments to Cresford from various investor proposals negotiated by the Cresford group ahead of limited partners, the allegations that representations had been made in the Subscription Documents and elsewhere that Cresford entities would be paid out of distribution after the "A" unit limited partners, that counsel for Cresford had confirmed that the intercompany loans were subordinated to the limited partners, that the General Partner had acted in breach of its fiduciary duties and that the Proposal was not being advanced in good faith; and
c. The timetable I approved on June 1 specifically contemplated the foregoing aspects of those applications being dealt with on June 23, 2021.

[36] If the related party claims are equity claims under the BIA, then it is also highly likely that the notional purchase price for the project being paid by the Proposal Sponsor under the Proposal must be viewed as being $22 million less than it might otherwise appear, a fact that is also material to the matters I must consider on this motion.

[37] The allegations of the applicant limited partners in the two outstanding applications challenge the good faith with which the Proposal has been advanced by the General Partner in part on the theory that the Proposal has in fact been advanced to secure payment of the related party claims in priority to the "A" unitholders and without securing their consent.

[38] For the foregoing reasons, I cannot avoid a consideration of whether the related party claims are equity claims. My conclusions on that subject are an integral part of any conclusion I must make on the subject of good faith or the criteria to be considered under s. 59(2) of the BIA.

[39] Are the related party claims identified by the Trustee in this case "equity claims"?

[40] The BIA contains a definition of "equity claims" that is deliberately non-exhaustive. In *Sino-Forest Corporation (Re),* 2012 ONCA 816 (CanLII) (at para. 44) the Court of Appeal found that the term should be given an expansive meaning to best secure the remedial intentions of Parliament.

[41] Subsequent cases have explored the concept of "equity claim" with a view to fleshing out its parameters. Some of the guidelines that can be distilled from that jurisprudence include the following:

a. Neither the "intention of the parties" as between non-arm's length parties nor the formal characterization they apply is conclusive as to the true nature of the transaction: *Tudor Sales Ltd. (Re),* 2017 BCSC 119 (CanLII) at para. 35 and *Alberta Energy Regulator v Lexin Resources Ltd*, 2018 ABQB 590 (CanLII) at para. 37.

b. The manner in which the transaction was implemented, and the economic reality of the surrounding circumstances must be examined to determine the true nature of the transaction with the form selected being merely the "point of departure" of the examination: *Lexin* at para. 37.

c. It is helpful to consider whether the parties to the transaction had a subjective intent to repay principal or interest on the alleged loan from the cash flows of the alleged borrower and, if so, was that expectation reasonable: *Lexin* at para. 41.

d. It is also helpful to consider the "list of factors" that courts have looked at in such cases – being careful not to apply them in a mechanical way or as a definitive checklist: *Lexin* at paras. 42-43.

e. Among the factors to examine are:

    i. the presence or absence of a fixed maturity date and schedule of payments (absence of such terms being a potential indicator of equity);

    ii. the presence or absence of a fixed rate of interest and interest payments. Again, it is suggested that the absence of a fixed rate of interest and interest payments is a strong indication that the advances were capital contributions rather than loans;

    iii. the source of repayments. If the expectation of repayment depends solely on the success of the borrower's business, the cases suggest that the transaction has the appearance of a capital contribution;

    iv. the security, if any, for advances; and

    v. the extent to which the advances were used to acquire capital assets. The use of the advance to meet the daily operating needs for the corporation, rather than to purchase capital assets, is arguably indicative of bona fide indebtedness: Lexin at paras. 42-43.

[42] The related party claims may be broken down into different buckets for the purposes of this analysis. The first one consists of payments that were made to retire loans taken out for the specific purpose of financing equity interests in YG LP. This

involved loans used to buy out the $15 million investment of a former limited partner, loans used to finance the Cresford group of companies' $15 million equity investment in Class B units as well as interest paid on both of these loans some or all of which has been recorded as obligations of YG LP on its books.

[43] Clearly advances made or charged to YG LP for the direct or indirect purpose of financing the purchase of an equity interest in YG LP are likely to the point of certainly to be characterized as equity claims of YG LP for the purposes of insolvency law. The evidence to this point supports the reasonable inference that a very substantial portion of the advances charged to YG LP by non-arm's length parties can be so characterized.

[44] A second category of advances made can only be described as "miscellaneous" comprised of various sporadic payments made by members of the Cresford group of companies that were recorded in the ledger of the limited partnership net of other payments made by the limited partnership to the Cresford group.

[45] The terms of the intercompany advances recorded on the general ledger of the limited partnership share the following characteristics:

a. They were all non-interest bearing without any defined term or maturity date; and

b. There are no loan documents evidencing any of them.

[46] Such payments as there were from YG LP on account of these advances were sporadic. The nature of the YG LP project is such that there is no cash flow nor any expectation of cash flow being available to repay the intercompany advances recorded until project completion when deposits and sales proceeds become available. The evidence does not suggest that intercompany advances were primarily short-term bridge advances pending the receipt of project financing that was to be used to repay them.

[47] There is substantial evidence that the related party advances were intended to be subordinated to holders of "A" units of YG LP and are thus equity claims. In the interest of time, I shall only summarize this evidence:

a. Direct written representations were made to the investors in YG LP "A" units as part of the subscription process that after payment of "project expenses" only "external lenders" debt would be repaid ahead of them and that distributions to "Cresford" – unambiguously referencing the group of companies rather than one entity – would come after repayment of invested capital and the agreed return on investment to the limited partner investors;

b. Cresford's communications to the limited partners never disclosed the existence of any "debt" owed to Cresford even when portraying "current debt" in various discussions with or disclosures made to them until very

recently (and long after the advances in question were recorded on YG LP's books);

c. Other Cresford group projects with similar capital structures also made representations that intercompany advances were treated as equity;

d. There was a direct, written representations made by prior counsel to the General Partner in October 2020 that such intercompany advances were "subsequent in priority" to the YG LP "A" unit investors – that admission has since been retracted without an adequate explanation for why it was an alleged error; and

e. Cresford's CFO also advised that the YG LP "A" unitholders would be paid in priority to "Cresford" a term used to describe the related group of Cresford companies under common control.

[48] A review of the foregoing factors in light of the jurisprudence leads me to the conclusion that the related party advances must be considered as equity claims for the purposes of this motion at least. Virtually all indicators reviewed point towards equity and there is little to no evidence leaning the other way.

(v) The implied value of the Proposal is $22 million less than assumed

[49] The Proposal operates to reduce the payments made to unsecured creditors if claims are lower than the $65 million cap. The converse is not the case. Absent the lien claims and the intercompany claims there is no mathematical prospect of the $65 million cap being operative unless the contingent and late-filed claims are resolved at levels far in excess of any reasonable estimate. This means that the consideration paid by Concord under the Proposal must be considered to be worth $22 million less than it might have been had the related party claims not been equity claims.

(vi) The general partner had authority to file the NOI

[50] The two groups of limited partners have raised three broad categories of objections to the capacity of the general partner to have filed the NOI and sought approval of the Revised Proposal: (i) as a matter of law, all partners including limited partners, must approve filing for bankruptcy; (ii) pursuant to the Limited Partnership Agreement, the general partner lacked the authority to file for bankruptcy; and (iii) the general partner ceased to be general partner prior to the filing. I shall consider each of these in turn.

S. 85(1) of the BIA

[51] Section 85(1) of the BIA provides that it "applies to limited partnerships in like manner as if limited partnerships were ordinary partnerships, and, on all the general

partners of a limited partnership becoming bankrupt, the property of the limited partnership vests in the trustee.”.

[52] The limited partners’ position was that since all partners of a general partnership must authorize a bankruptcy filing and since s. 85(1) of the BIA applies the law in relation to general partnerships to limited partnerships in “like manner”, it follows that an NOI must be authorized by all limited partners in addition to the general partner. In support of this interpretation they cite the case of *Aquaculture component Plant V Limited Partnership (Re)*, 1995 CanLII 9324 (NS SC) where two NOI’s filed on behalf of limited partnerships were annulled on this basis.

[53] While the decision of Hamilton J. in the *Aquaculture* case is entitled to deference, it is not binding upon me. I find that I am unable to agree with its reasoning.

[54] The *Aquaculture* case stands quite alone in the jurisprudence on this topic – alone in the sense that none appear to have followed *or* disagreed with it as far as the research conducted by the parties has been able to determine. In the 26 years since it was decided, a significant number of limited partnerships have passed through our bankruptcy courts either for proposals or liquidations without apparent objection on this score. That practice of course does not have the effect of altering the law but it is at least a factor to consider given the number of times since then that Parliament has examined the BIA including with the addition of s. 59(4) that authorized changes to the constating documents of a debtor including a limited partnership.

[55] I reach a different conclusion than was reached in *Aquaculture* for the following reasons:

a. The use of general “in like manner” language in s. 85(1) of the BIA is intended to ensure that the provision is interpreted consistent with the objects of the BIA and not in a manner as to defeat those objects or render the benefits of the BIA largely inaccessible to limited partnerships. The procedure for filing an NOI was intended to offer debtors a swift and relatively low cost means of seeking creditor protection after a secured creditor gives the required ten-day notice of its intention to enforce. Requiring unanimous consent for filing of an NOI would have the practical effect of making the benefits of bankruptcy law unavailable to limited partnerships in practice in a large number of cases. Limited partnerships often have large numbers of limited partners and the time required to convene a meeting and obtain unanimous consent would require more time than secured creditors are required by law to give in the way of notice.

b. Provincial law generally provides that only general partners may bind a limited partnership (in Manitoba, s. 54(1) of the *The Partnership Act*, CCSM c P30) and the BIA treats partnerships and limited partnerships as a full

"debtor". The policy behind requiring all *general* partners to authorize a bankruptcy filing is obvious – all are liable without limit for the liabilities of the partnership. The same is not the case with a limited partnership.

c. Section 59 of *The Partnership Act* also provides that actions or suits in relation to the limited partnership may be brought and conducted by and against the general partners as if there were no limited partners. This too supports the proposition that the consent of limited partners is not required for the filing of an NOI on behalf of the partnership.

[56] I find that s. 85(1) of the BIA did not require the asset of each limited partner to the filing of an NOI.

[57] The limited partners also pointed to provisions of the Limited Partnership Agreement to allege that the General Partner had automatically ceased to be general partner of the partnership by reason of certain actions or that that it lacked the authority to file on behalf of the partnership.

Did the General Partner cease to be a general partner of YG LP at any time?

[58] The Proposal Sponsor Agreement is dated April 30, 2021 and was entered into between Concord as Proposal Sponsor and YG LP acting through the General Partner. It was executed prior to filing the NOI but *after* the two limited partner groups had filed their separate applications seeking, among other things, to remove the General Partner. To the extent it is relevant, there can be no question but that Concord was aware of the terms of the Limited Partnership Agreement at all relevant times when negotiating and entering into the Proposal Sponsor Agreement.

[59] Pursuant to s. 1.1 of the Proposal Sponsor Agreement, YG LP agreed to "use commercially reasonable efforts to effect a financial restructuring of [YG LP] that will result in the acquisition of the Property by the Proposal Sponsor together with [YG LP's] rights, title and interests in and to such Project-related contracts as may be stipulated". A draft of a proposal, substantially similar to the Proposal before this court for approval, was appended as a schedule to the Proposal Sponsor Agreement. The agreement was signed by Mr. Daniel Casey on behalf of each of the Cresford companies named as parties including YG LP.

[60] Section 10.14 of the YG LP Limited Partnership Agreement provides that "None of the following actions shall be taken unless it has *first* been approved by Special Resolution: (a) approving or disapproving the sale or exchange of all or substantially all of the business or assets of the Partnership"(emphasis added).

[61] The Proposal contemplated by the Proposal Sponsor Agreement clearly provides for the sale or exchange of all or substantially all of the business or assets of the Partnership. Section 1.1 of the Proposal Sponsor Agreement obliged YG LP to "use

commercially reasonable efforts" to cause this to occur, including by filing the NOI and to requesting court approval of the Proposal. As obliged by the Proposal Sponsor Agreement, YG LP filed an NOI, filed the Proposal and subsequently sought court approval of the Proposal.

[62] Entering into the Proposal Sponsor Agreement constituted the "approval" of YG LP to the sale or exchange of all or substantially all of the business or assets of the Partnership" even if approvals of other parties were also required in order to *complete* the transaction. The prohibition in art. 10.14(a) attaches to the approval of the action and not its completion.

[63] Section 7.1(c) of the Limited Partnership Agreement creates an Event of Default if the General Partner "becomes insolvent … consents to or acquiesces in the benefit of [the BIA]". By filing the NOI as a general partner of YG LP, the General Partner necessarily admitted to being insolvent at the time the NOI was filled out. There is no evidence that such state of insolvency arrived suddenly that day. The General Partner has accordingly admitted to the existence of an insolvency default under s. 7.1(c) of the Limited Partnership Agreement at some time prior to filing the NOI failing which no NOI would have been possible. By signing the Proposal Sponsor Agreement and agreeing to file the NOI to advance the Proposal, the General Partner also consented to the receiving the benefit of the BIA proposal provisions.

[64] For all of the foregoing reasons, the signing of the Proposal Sponsor Agreement amounts to an admission of further breaches of the Limited Partnership Agreement.

[65] Do such breaches entail the automatic removal of the authority of the General Partner to act as such at the time the NOI was actually filed? The answer in my view is that none of them have that effect.

[66] Section 11.2 of the Limited Partnership Agreement concerns the removal of the General Partner. Pursuant to s. 11.2(a), the General Partner "'may be removed" by a court of competent jurisdiction on certain named grounds. That has not occurred. Section 11.2(b) provides that the General Partner "shall cease to be general partner" if any of the named events occurs. None of the agreement to file an NOI, the state of being insolvent or the signing of the Proposal Sponsor Agreement can be read to be included in the list of events listed in s. 11.2(b). The *aftermath* of the filing of the NOI may well be such a trigger but the answer to that question would require me to contend with the effects of the automatic stay which has not been raised before me.

[67] Accordingly, I find that the NOI filed by the General Partner was not void or subject to any similar infirmity. The foregoing conclusion refers only to the actual filing of the NOI and specifically does not apply to the breaches of the Limited Partnership Agreement consequent upon entering into the Proposal Sponsorship Agreement discussed above.

(vii) The Proposal was the product of a flawed process and breaches of fiduciary duty by the General Partner

[68] There are two aspects to this part of the objections raised by the objecting limited partners. First, it is alleged that during the year leading up to the Proposal Sponsor Agreement, the General Partner breached its fiduciary duty to act in the best interests of the partnership by seeking to advance the interests of non-arm's length parties to the detriment of the limited partners while simultaneously frustrating every effort of the limited partners to access the information that the Limited Partnership Agreement and the Manitoba *Partnership Act* gave them the rights to see. Second, it is alleged that negotiating and entering into the Proposal Sponsor Agreement was a breach of fiduciary duties of the General Partner in that this was nothing less than deliberately negotiating and entering into an agreement to breach the Limited Partnership Agreement.

[69] As the sole general partner of YG LP, the General Partner was responsible for the management of the affairs of the limited partnership and was the only one able to bind the partnership. The General Partner owed a fiduciary duty to all of the partners of the firm in discharging that role and pursuant to s. 64 of *The Partnership Act*, is liable to account, both at law and in equity to the limited partners for its management of the firm.

[70] As I have outlined above, entering into the Proposal Sponsor Agreement was a clear violation of s. 10.14 of the Limited Partnership Agreement as it agreed to a process whereby substantially all of the property of the firm would be conveyed to a third party without the assent of the limited partners. The fact that the BIA stay of proceeding may impede or prevent the limited partners from seeking a direct remedy for that breach when the agreement was subsequently put into action by filing the NOI does not detract from the existence of a present breach the moment pen was put to paper. Further, whether the negotiations of the Proposal Sponsor Agreement consumed two weeks or two months, it was a breach of fiduciary duty to plan and then put into execution a deliberate breach of the Limited Partnership Agreement and doing so in the teeth of a pending application to stop the General Partner adds further weight to that conclusion.

[71] The debtors suggested that being in the proximity of insolvency dissolved or altered the fiduciary duties of the general partner owed to the limited partners. It is true that the law recognizes that the interests of creditors assume a greater weight the closer to insolvency the enterprise approaches. None of this dissolves the fiduciary obligations of the General Partner so much as it adds to them. It is at this point that the other aspect of the complaint of the limited partners enters the analysis.

[72] Nothing in what I have written suggests that a general partner cannot file an NOI where doing so appears on all of the facts and in the good faith exercise of the best business judgment of the general partner to be in the best interests of the enterprise as a whole to do so – a judgment that necessarily accounts for the obligations of the firm owed to its creditors.

[73] This filing was different because it came with strings attached: a binding Proposal Sponsor Agreement that granted exclusivity to a single party and obliged the General Partner to pursue one path and one path only to emerge from the process. Those strings did not get attached as a result of a process which itself discharged faithfully the fiduciary duties of the General Partner. Rather they were attached as the culmination of almost a year of battling to keep information away from limited partners that they had a right to access (in most cases at least) and the squandering of an expensively purchased window of restructuring breathing room looking not for the solution best able to discharge all of the obligations of the partnership but rather looking for the investor best able to secure the optimal outcome for the Cresford group of companies generally. In that process the limited partners were an obstacle to be circumvented and bankruptcy provided a possible key.

[74] Good faith in such circumstances is not assumed but must be shown. The evidence presented to me has rather persuasively convinced me that good faith took a back seat to self-interest.

[75] The parties have expended considerable effort in outlining the details of what occurred in that time frame. In the interests of time, I shall summarize the important take-aways from those events:

a. Until the Proposal Sponsor Agreement and the April 2021 CBRE report prepared for Concord, *all* appraisal evidence showed a profitable project likely to result in full coverage for all of the outstanding third-party debt obligations plus all of the obligations owed to limited partners;

b. The General Partner presented two potential transactions to the “A” unit limited partners in the second half of 2020 that provided for the full payment of all debt, the payment of approximately $38 million to non-arm’s length parties related to the General Partner and payment of obligations owed to the limited partners at a discount – the latter of the two proposals emanated from Concord;

c. The two proposals failed to proceed primarily because the General Partner was unable to provide a satisfactory explanation as to why Cresford related parties were to receive a substantial payment when limited partners were asked to accept a compromise the obligations due to them and limited partners had been assured that Cresford group obligations ranked behind them both when they made their investment and as late as October 2020 in a letter from counsel the debtors; and

d. The limited partners were in a continual tug-of-war trying to pry information out of the General Partner having had to resort to a court order at the

beginning of this year to obtain access to information that should have been available to them as of right.

[76] Few things are more precious in the restructuring business than time. YG LP was able to "purchase" more than a year of time with the forbearance arrangements that it worked out. That precious time appears to have been devoted solely to finding transactions that offered the greatest level of benefits for the Cresford group of companies. There is no evidence that any canvassing of the market – however constrained the market of developers capable of undertaking the completion of an 85-story mixed use tower in downtown Toronto may be – took place that was not indelibly tainted by the imperative of finding value for the Cresford group of companies rather than for the partnership itself.

(viii) The Affected Creditor vote was unanimous

[77] Despite the fact that I have found that fifteen of the forty-six votes cast in favour of the Proposal ought not to have been considered because they came from Unaffected Creditors, that determination does not impact the conclusion of the Trustee that the required statutory majorities voted in favour of the Proposal. There was but one negative vote cast and the Trustee disallowed that vote as being contingent. I have reviewed the Trustee's reasons for so ruling and find no fault with them. The removal of fifteen creditors and just over $9 million in claims does not detract from the fact that thirty-one creditors holding approximately $9 million in other claims cast votes in favour.

[78] While I am prepared to consider to some degree the impact of the assignment agreements negotiated by Concord (see below), I do not view such agreements as impacting the formal validity of the votes cast.

[79] I find that the Proposal received the required majority of two-thirds in value and over 50% in number of creditors voting in person or by proxy.

(ix) The probative value of most of the Affected Creditor vote is attenuated

[80] In the normal course, the agreement of a broad group of creditors to accept less than 100% of what they are owed is cogent evidence of the fairness and reasonable nature of a proposal. This is so as a matter of common sense and by a very long tradition in our law. It is not an indicator lightly to be ignored.

[81] I must also recognize that whatever doubts the evidence may raise as to the insolvency of the debtors in terms of the realizable value of their assets, there can be little doubt that the liquidity test for insolvency is met. The lien claimants have been unpaid for a year or more without any formal forbearance agreement. The first mortgagee has entered into a forbearance agreements but this expires on June 30, 2021.

[82] There was a window of time to find an out-of-court solution, but it would appear that the debtors have squandered it.

[83] The vote of the Affected Creditors *is* probative of fairness, but I find that its weight is attenuated in this case by the following circumstances:

a. Only a relatively small minority voted who did not also enter into assignment agreements;

b. The evidence is equivocal about precisely what consideration was received by those who entered into such assignment agreements – a relayed denial of "side-deals" without more adds little to the equation particularly when the deal itself is not disclosed;

c. Clearly if assigning creditors received or stand to receive more than the value allocated to them under the Proposal, their positive vote says little about the business judgment of the creditors at large to accept the value offered to satisfy their claims but says more about the willingness of the Proposal Sponsor to pay more than has been reflected in the Proposal itself.

d. This last-in-line class of creditors did not have available to it the range of information produced in connection with this approval motion.

Disposition

[84] I will not approve the Proposal in its present form. I have concluded that, as presented, the Proposal is not reasonable, it is not calculated to benefit the general body of creditors and there are serious issues regarding the good faith with which it has been prepared and presented by the debtors. The debtors and the Proposal Sponsor have the authority under art. 3.06 of the Proposal to amend the Proposal to address the concerns I have raised. It is up to them – with the approval of the Trustee – to do so if they are so inclined.

[85] I am directing the parties to return on Wednesday June 30 at 2:15 pm either to propose amendments to the Proposal that address the concerns I have raised in a substantive way or to address next steps.

[86] These written reasons expand upon the summary reasons I presented orally in a hearing on June 29, 2021. I have released these reasons with relatively little opportunity to proof them and correct typographical errors or minor nits or stylistic glitches. I shall do so over the next week when I have more time available to me and the capacity to call upon my able assistant Ms. Daisy Ng to assist in that effort. Accordingly, I shall be releasing an amended version of these reasons over the course of the next week with such minor and non-substantive corrections.

_____

S.F. Dunphy J.

Date: June 29, 2021

The foregoing is the corrected text of my reasons. Orphaned words have been removed or obvious missing words restored along with corrections of minor errors only. The parties have received a blackline version to compare the changes. Since releasing these reasons, I have adjourned the hearing scheduled for June 30, 2021 at 2:15 until July 9, 2021 at 10:00am. In so doing, I issued the following additional directions:

> As KSV Restructuring Inc. ("KSV") will become the bankruptcy trustee and court-appointed receiver on July 9, 2021 if no satisfactory amended proposal is approved at that time, this Court hereby authorizes and directs KSV to undertake the steps towards formulating a sales process that it would be undertaking if it had been appointed the receiver today.
> KSV's costs of doing so from July 1, 2021 shall be deemed costs of the receiver upon the granting of a receivership order on July 9, 2021 failing which all such costs will be deemed to be costs of the Proposal Trustee in the proposal proceeding.

Issued: July 2,2021

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S.F. Dunphy J.

TAB 28

CITATION: YG Limited Partnership and YSL Residences (Re), 2021 ONSC 5206
COURT FILE NOS.: CV-21-00655373-00CL/BK-21-02734090-0031, CV-21-00661386-00CL & CV-21-00661530-00CL
DATE: 20210716

SUPERIOR COURT OF JUSTICE – ONTARIO
(COMMERCIAL LIST)

RE: IN THE MATTER OF THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, C. B-3, AS AMENDED

AND:

IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF YG LIMITED PARTNERSHIP AND YSL RESIDENCES

APPLICATION UNDER THE *BANKRUPTCY AND INSOLVENCY ACT*, R.S.C. 1985, C. B-3, AS AMENDED

AND RE: 2504670 CANADA INC., 8451761 CANADA INC. and CHI LONG INC., Applicants

AND

CRESFORD CAPITAL CORPORATION, YSL RESIDENCES INC, 9615334 CANADA INC., YG LIMITED PARTNERSHIP and DANIEL CASEY, Respondents

AND RE: 2583019 ONTARIO INCORPORATED AS GENERAL PARTNER OF YONGESL INVESTMENT LIMITED PARTNERSHIP, 2124093 ONTARIO INC., SIXONE INVESTMENT LTD., E&B INVESTMENT CORPORATION and TAIHE INTERNATIONAL GROUP INC., Applicants

AND

9615334 CANADA INC. AS GENERAL PARTNER OF YG LIMITED PARTNERSHIP and YSL RESIDENCES INC., Respondents

BEFORE: S.F. Dunphy J.

COUNSEL: *Harry Fogul* and *Miranda Spence*, for YG Limited Partnership and YSL Residences Inc.

Shaun Laubman and *Sapna Thakker*, for 2504670 Canada Inc., 8451761 Canada Inc., and Chi Long Inc.

Alexander Soutter, for YongeSL Investment Limited Partnership, 2124093 Ontario Inc., SixOne Investment Ltd., E&B Investment Corporation, and TaiHe International Group Inc.

David Gruber, Jesse Mighton, and *Benjamin Reedijk,* for Concord Properties Developments Corp. and its affiliates

Jane Dietrich and *Michael Wunder,* for 2292912 Ontario Inc. and Timbercreek Mortgage Servicing Inc.

Robin B. Schwill, for KSV Restructuring Inc. in its capacity as the proposal trustee

Roger Gillot and *Justin Kanji,* for Kohn Pedersen Fox Associates PC

Reuben S. Botnick, for Royal Excavating & Grading Limited COB as Michael Bros. Excavation

Jamie Gibson, for Sarven Cicekian, Mike Catsiliras, Ryan Millar and Marco Mancuso

Brendan Bowles, for GFL Infrastructure Group Inc.

Mark Dunn, for Maria Athanasoulis

James MacLellan and *Jonathan Rosenstein,* for Westmount Guarantee Services Inc.

Albert Engle, for Priestly Demolition Inc.

HEARD at Toronto: July 9 and 16, 2021

REASONS FOR DECISION #2 (REVISED PROPOSAL)

[1] On June 29, 2021, I rejected the debtor's application for approval of its Proposal (identified as "Amended Proposal #2) and provided my detailed reasons for doing so on July 2, 2021. In delivering my reasons, I indicated that that it remained possible for the debtors to amend their Proposal if they so chose. The debtors for their part asked me to adjourn the hearing until July 9, 2021 in order to permit them an opportunity to do so. I granted the requested adjournment.

[2] An amended proposal was filed immediately prior to the hearing on July 9, 2021 entitled "Amended Proposal #3" and I have been asked to consider approving such

Amended Proposal. I held a hearing on whether Amended Proposal #3 ought to be approved on July 9, 2021. Amended Proposal #3 was filed only a short while prior to that hearing. I delayed the start of the hearing for an hour to give parties time to review and analyse the document and proceeded to hear their submissions.

[3] As is usual, I called upon the Trustee to give its comments last. The Trustee requested a further week to review the document and to consider its position. I granted that request and the matter was adjourned to July 16, 2021 at 10:00 a.m. This second adjournment was granted – it must be noted – over the objections of the 1st mortgagee Timbercreek whose forbearance agreement with the debtors expired on June 30, 2021 and who has a long-standing hearing date for its receivership application on July 12, 2021. I adjourned the Timbercreek July 12, 2021 hearing to July 16, 2021 as well such that both proceedings were scheduled to appear before me on July 16, 2021.

[4] A term of the adjournment I granted was that the debtors and Timbercreek should both have circulated draft orders (Proposal approval order in the case of the debtors; Receivership Order in the case of Timbercreek) in advance of the hearing on July 16, 2021 with the expectation that I should sign one of the two orders on July 16, 2021.

[5] On July 15, 2021, a second version of Amended Proposal #3 was filed with the Official Receiver and the Trustee issued its Fourth Report commenting on version 2 of Amended Proposal #3. The Trustee's Fourth Report recommended approval of the Proposal as so amended.

[6] This Proposal has been through a few versions and the nomenclature can get confusing. The amendments made in version 2 of Amended Proposal #3 were minor and technical in nature – they did not adversely affect the rights of any Affected Creditor and at least one of them could just as easily have been added to the approval order outside of the Proposal without objection. My references to "Amended Proposal #3" below should be taken as referencing version 2 of Amended Proposal #3 unless the context requires otherwise.

[7] For the reasons that follow, I have decided to approve version 2 of Amended Proposal #3 and I have signed the approval order.

Background facts

[8] I shall not repeat my review of the facts nor my reasons for rejecting Amended Proposal #2 on June 29, 2021. My detailed reasons for that decision were released on July 2, 2021 and should be considered as if incorporated by reference herein.

[9] In broad strokes, the following summarizes the principal amendments made in Amended Proposal #3:

a. Lien claimants who assigned their claims to the Proposal Sponsor ($9.2 million) will not share in the pool of cash available to unsecured creditors under the Proposal – all lien claimants will be treated as Unaffected Creditors;

b. Related party claims ($38.3 million) will be treated as equity claims and not participate in the pool of cash available to unsecured creditors;

c. Unsecured creditors' recoveries will no longer be limited to $0.58 per dollar of proven claim but will share *pro rata* in the pool of cash available to unsecured creditors up to payment in full;

d. The Proposal Sponsor will fund the full cash pool on Proposal Implementation without reduction should proven claims come in below the amount of the cash pool ($30.9 million);

e. The pool of cash available to unsecured creditors is reduced from $37.7 million to $30.9 million but subject to the above changes reducing the claims eligible to share in the pool;

f. Secured creditors claims – including all construction lien claims – remain unaffected and are assumed by the Proposal Sponsor in purchasing the land and project assets;

g. After Affected Creditor claims have been resolved and all required payments made to them, any residual amount will be returned to the debtor YG Limited Partnership to be dealt with as the partners direct or the court orders; and

h. Proposal Implementation will occur three days after court approval.

[10] The Fourth Report of the Trustee summarized the impact of these changes. Some of the principal points made by the Trustee include the following:

a. Construction lien claimants who agreed to assign their claims to the Proposal Sponsor prior to these amendments might potentially receive less under their assignment agreements than they would under Amended Proposal #3 which had not been made when they agreed to assign their claims. The Trustee contacted the assigning creditors. Two were unable to be contacted but have voiced no objection one way or the other. The remainder of them expressed support for the approval of Amended Proposal #3 or made no objection to it. No assigning creditor was opposed.

b. Version 2 of Amended Proposal #3 contains material improvements to Amended Proposal #2 and addresses concerns raised in my decision of June 29, 2021.

c. Any payments to equity holders are entirely outside of the Proposal.

d. The Trustee has analyzed the known unsecured claims that would share in the $30.9 million pool available to Affected Creditors under Amended Proposal #3. The Trustee's estimate is that Affected Creditors will receive between 71% of their claims and payment in full under version 2 of Amended Proposal #3 as contrasted with between 40% and 58% of their claims under Amended Proposal #2. The lower assumption is based on all known claims being allowed in full as claimed with an identical estimate for claims not yet filed. In the event none of the disputed or contingent claims were allowed, the Affected Creditors would be paid in full and up to $19 million may be available to holders of equity claims.

[11] Amended Proposal #3 came with an additional element that the Proposal Sponsor felt it proper to disclose to the Court and the parties. The Proposal Sponsor made a parallel and entirely voluntary offer to holders of limited partnership units in YG LP as well as other claims found by me to be equity claims (i.e. the related party claims) to sell their equity interests for 12.5% of the value of such interests subject to certain structuring conditions.

[12] I cannot say at this juncture whether any equity holders will take the Plan Sponsor up on this offer. The objecting limited partners have shown little interest in it to date at least. The offer has conditions that may or may not be acceptable to them depending upon their own tax situation and their views of value.

[13] Fifty years after the Carter Commission report, it remains the case that business transactions are invariably structured to minimize tax which continues to impact similar economic transactions differently depending upon the structures used. I am satisfied that the "equity offer" is not a disguised transfer of value from creditors to holders of equity claims – the structures required to be used potentially deliver tax attributes to a buyer of the claims that would not otherwise be available. This proposal has been properly disclosed but I do not view it as being particularly relevant to my assessment of Amended Proposal #3. That proposal delivers additional value to creditors under all scenarios compared to its predecessor. There is no diversion of value from creditors to equity holders to be found here. I concur with the Trustee's assessment that the equity offer is quite independent of the Proposal and does not contravene the *BIA* provisions against payment to equity ahead of debt even if it turns out that creditors receive less than payment in full (and that would be a fairly speculative assumption to make).

[14] The Trustee's Fourth Report concluded that the Debtors were proceeding with the request for approval of the Amended Proposal #3 in good faith.

Analysis and discussion

[15] This amended proposal is not perfect. The process that led to it was far from ideal. However, as now amended, this Proposal provides a superior outcome for all classes of creditors under every conceivable scenario and addresses all of the concerns raised in my reasons of July 2, 2021 constructively and substantively.

[16] As so amended, I have no hesitation in finding that Amended Proposal #3 is reasonable, it is calculated to benefit the general body of creditors and is being advanced at this juncture in good faith notwithstanding the defects that I found marred the negotiation and presentation of the initial version of the Proposal.

[17] There were some critical foundational findings that I made in my reasons of July 2, 2021 including:

a. whatever breaches of the Limited Partnership Agreement may have occurred in the weeks and months prior to the filing of the NOI, the general partner *did* have authority to file the NOI;

b. the Affected Creditor vote in support of Amended Proposal #2 was in fact unanimous; and

c. whatever questions there may be regarding the solvency of the debtors from the perspective of the realizable value of their assets, there can be no question of the insolvency of the debtors from a liquidity point of view: secured and unsecured claims alike are overdue and unpaid and the debtors have no means to satisfy their claims in a timely way. Lien claims are more than a year in arrears for the most part while all forbearance periods have expired for the secured debt.

[18] While I found the probative value of the creditor vote to be attenuated somewhat by the factors I listed in those reasons, the vote did and does have probative value and it is material to note that unsecured creditors agreed to accept payment of less than full payment on their claims on June 15, 2021. All of the Affected Creditors will receive a superior outcome under Version 2 of Amended Proposal #3 under any reasonable assumptions. Their approval of the prior version of the Proposal remains as probative in the context of version 2 of Amended Proposal #3 if not more so.

[19] Version 2 of Amended Proposal #3 clearly satisfies the technical requirements of the *BIA* in that Amended Proposal #2 upon which the creditors did vote authorized the amendments that have been made in Amended Proposal #3 (including version 2 thereof).

[20] Version 2 of Amended Proposal #3 has constructively addressed each of the issues I raised in my June 29 ruling and my July 2 written reasons:

a. The construction lien claims will not dilute the recovery of the unsecured creditors in any way.

b. The related party claims are to be treated as equity claims and disentitled to share in the cash pool.

c. While I expressed grave concerns regarding the lack of good faith and the breaches of fiduciary duty that preceded the filing of the NOI and the entry into the Proposal Sponsor Agreement, those concerns were primarily focused on the efforts made to prefer related party claims over those of other stakeholders in the search for an investor. Amended Proposal #3 cannot undo the past of course but it has addressed those findings constructively. The related party claims are treated as equity claims.

d. There is a strong likelihood that proven creditor claims will be substantially lower than the $30.9 million pool available to satisfy them and Amended Proposal #3 ensures that such surplus is returned to the limited partnership instead of being retained by the Proposal Sponsor.

e. The claims of related parties and their priority relative to limited partners will be dealt with within the limited partnership structure itself, in broad daylight and subject to the full range of remedies open to the limited partners to protect their interests should the need arise. The conflicting interests that marred the development of Amended Proposal #2 have been substantially cured by the amendments effected by Amended Proposal #3. Related parties have been put in their proper place in the claims hierarchy.

[21] The strongest critique levelled at Amended Proposal #3 by the limited partners is that it does not answer the question of what the value of the project might have been had the project been offered on the open market in a competitive process. That is a fair criticism but not one that is sufficient to detract from the overwhelmingly positive attributes of this Proposal.

[22] The past cannot be undone and perfection is not the standard against which a proposal is to be measured. Section 59(2) of the *BIA* requires that approval of a proposal must be refused if its terms are not shown to be reasonable and calculated to benefit the general body of creditors. The common law has added to this the requirement that a proposal must be advanced in good faith.

[23] Amended Proposal #3 is both reasonable and calculated to benefit the general body of creditors. It provides for substantially improved outcomes to all creditors whose

claims were impaired by Amended Proposal #2 under any reasonable assessment of the facts. As noted above, it is quite likely that a surplus will remain to be returned to the limited partnership after all affected unsecured claims have been paid in full to be dealt with as the limited partners direct (or by court order if necessary).

[24] The debtors are insolvent today. They are properly in bankruptcy proceedings. Their creditors have a right to payment and – to the extent reasonably possible – to payment in full as soon as possible. Amended Proposal #3 offers payment in full to most secured creditors within a matter of days following court approval. Unsecured creditor payments will be subject to reasonable reserves for unresolved claims but these too will begin flowing in short order. This contrasts to a delay of *many* months on the most optimistic of scenarios were a receiver directed to sell the project.

[25] There is a public interest in moving this very substantial project out of the quicksand in which it has become stuck for over a year. Approval of Amended Proposal #3 at this juncture ensures that the Project is in the hands of a solvent entity with the wherewithal and experience necessary to put it back on track as soon as possible.

[26] The real question before me today is whether limited partners have the right to require creditors to run the risk of a sale process producing an inferior outcome to Amended Proposal #3 in order to test the hypothesis that a greater value might emerge from a fresh marketing of the project in a liquidation process that might result in payment of some or all of the limited partners' equity claims. In my view, they do not.

[27] It is possible that higher values could emerge from a liquidation process but that possibility is not a one way street. The dissatisfaction I expressed in my reasons of July 2, 2021 regarding the quality of the appraisal evidence before me does not imply any level of probability that market value today is *higher* than the values suggested by the April 2021 CBRE appraisal. I was dissatisfied with the quality of *all* of the appraisal evidence because of the lack of evidence reconciling the differences between them and, in particular, assessing the reasonableness of the assumptions made in each.

[28] It is noteworthy that version 2 of Amended Proposal #3 offers the real prospect that a return on equity of more than 100% of the invested capital of the limited partners may come back to YG LP. The limited partners assent will be needed to any use of those funds unless a court order is obtained. The possible upside to limited partners arising from a new sales process has thus become that much more remote under this last revision to the Proposal compared to the first.

[29] There are costs involved in conducting a receivership that would come ahead of any potential surplus being made available to equity claimants such as the limited partners. Some of the risk of a sale process producing a lower outcome could potentially be insured against by procuring a stalking horse bid to put a floor under the sale process.

There is no guarantee that a stalking horse bid would be available at or near the implied value of Amended Proposal #3. Stalking horse bids come with a price tag in the form of a break fee that is usually calculated as a percentage of the price. That too would stand to reduce the recoveries to unsecured creditors and create an additional hurdle to any prospect of additional recovery to limited partners.

[30] This is a real bankruptcy. There is nothing artificial about it. Creditors have been unpaid for over a year. I have before me a transaction that provides a pathway to payment of creditor claims in full and quickly while leaving a realistic prospect for equity claims to receive some significant recovery. Every other option requires the creditors – who bear no responsibility for the mess that this project has found itself in – being subjected to the real risk of partial non-payment and substantial delay being added to the very lengthy delay to which they have already been subjected in order to test the hypothesis that a few percentage points of additional value might potentially be found. That is not a risk that it is fair to impose on creditors on these facts and having regard to the important favourable changes made to the Proposal.

Disposition

[31] Accordingly, an order shall issue approving version 2 of Amended Proposal #3. I have reviewed the draft form of approval order uploaded and approved and signed same. It was amended slightly to include in the preamble corrected references to the limited partners who appeared and the evidence they filed.

[32] This Proposal satisfies the technical requirements of the *BIA*. I have concluded that version 2 of Amended Proposal #3 represents a valid amendment to Amended Proposal #2 in accordance with its terms and thus has received the required double majority of creditor approval. The terms of this Proposal are reasonable and calculated to benefit the general body of creditors. The amendments presented have satisfied the concerns raised by me regarding the good faith of the debtors in pursuing *this* Proposal.

[33] I wish in particular to note that I have included, as requested, an order pursuant to s. 195 of the *BIA* permitting provisional execution of the approval order notwithstanding appeal. I have made this order in consideration of two primary factors:

a. The secured creditors of YG LP have been deferred and stayed for a very, very long time at this point. Some of that deferral was purchased in the form of forbearance agreements with Timbercreek but the last negotiated extension – an extension that included every possible assurance that no further extensions would be sought – expired on June 30, 2021. I made it clear on July 9, 2021 that I would be approving the Proposal or a Receiver today. It would be unjust to Timbercreek to have its period of limbo indefinitely extended by the simple expedient of filing a Notice of Appeal and forcing Timbercreek to seek a lifting of an automatic stay to enforce its

security. This project is, at its core, a hard asset consisting of real estate, a bundle of approvals and a hole in the ground. There is no goodwill to speak of. It has been held in limbo for much more than a year at this point and it must either be put in the hands of someone who will bring it forward to completion under the Proposal or of a Receiver who will find someone who can.

b. Our courts have generally sought to achieve a degree of uniformity of practice as between the CCAA and the *BIA*. Approval of a CCAA Plan Is not subject to an automatic stay. An automatic stay in this case would operate as a functional veto of the Proposal itself because the result would be an almost certain slide into receivership unless the stay were promptly lifted.

[34] Timbercreek's receivership application was adjourned by me from July 12, 2016 until today. Based upon my approval of the Proposal today *and subject to the closing of version 2 of Proposal #3 in accordance with its terms by no later than July 31, 2021*, Timbercreek agrees that its application is moot. There is no reason to believe the Proposal will not be completed as planned, however, nothing can be taken for granted. I am adjourning Timbercreek's application to August 9, 2021 when I shall next be sitting. It is adjourned before me.

[35] Assuming (i) the Trustee confirms to me that the version 2 of Amended Proposal #3 has been completed and (ii) Timbercreek does not advise me in advance of August 9 of its intention to proceed, I shall endorse the Timbercreek application as withdrawn without costs on August 9, 2021. No attendances will be necessary from any party in that eventuality. If there is a reason for the application to move forward, I am relying on the Trustee and Timbercreek to so notify me as soon as practicable after July 31, 2021.

[36] A request was made by the limited partners to make submissions to me regarding costs of the bankruptcy proposal proceeding. For the avoidance of doubt, my signing of the order approving version 2 of Amended Proposal #3 has not disposed of the matter of costs of the proposal proceedings. I have made no order as to costs to this point nor have I heard submissions on the point.

[37] Any party seeking an order of costs in their favour shall have ten days from today to file written submissions and an outline of costs. Submissions should not exceed ten pages excluding the outline of costs. Cases need not be included beyond a hyperlinked table of cases. The Debtors and the Proposal Sponsor shall each have a further ten days to respond to any such requests for costs with similar size restrictions. All submissions are to be uploaded to CaseLines and copied to the Trustee. I am asking the Trustee to provide me with a consolidated set of submissions to which the Trustee may – but shall

not be required to – add its own additional comments in the form of a brief supplementary report.

[38] Lastly, I need to give some directions regarding the two civil applications that immediately preceded these bankruptcy proceedings brought by the limited partners of YG LP. My reasons of June 29, 2021 made a number of findings in relation to matters raised in those two applications. However, it must also be clear that neither my ruling of June 29, 2021 nor this decision has fully disposed of either civil application.

[39] It is certainly true that I made findings in the context of the bankruptcy proposal proceedings that were and are relevant to the two applications. Even if those findings were made in the context of the bankruptcy proceedings, the three proceedings were to a degree inextricably intertwined. I was asked to issue a formal order in relation to the findings I did make. I declined to do so not because I am resiling from any findings made – I do not – but because I did not and do not have the full scope of the claims of either application fleshed out before me. I directed certain matters to be explored and argued due to the interrelationship between the proceedings but I do not want my rulings in one context to be taken out of context in another.

[40] The safest course in my view is to let my rulings stand as made knowing that *res judicata* and issue estoppel can be applied as needed to avoid any abuse. I was asked to confirm – and do so now – that costs of those two civil applications have not been dealt with by me at all. They have not. The limited partner applicants in those two proceedings asked to make submissions regarding costs of the bankruptcy proposal proceeding and I have given them leave to do so as provided above. The costs of the two civil applications remain reserved to the judge disposing of them.

_____

S.F. Dunphy J.

Date: July 16, 2021

Addendum:

As noted, I have reviewed the originally signed reasons and made a small number of clerical and stylistic changes to the text as originally released. As well, I was advised by the Trustee that the transaction was in fact completed on July 22, 2021. Accordingly, I

have issued an endorsement today vacating the August 9, 2021 appointment reserved to hear the Timbercreek application and endorsed that matter as being abandoned without costs because moot. No party will be required to appear on August 9, 2021.

Date: July 27, 2021

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S.F. Dunphy J.

TAB 29

DEBTORS AND CREDITORS SHARING THE BURDEN:

A Review of the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act*

Report of the Standing Senate Committee on Banking, Trade and Commerce

Chair
The Honourable Richard H. Kroft

Deputy Chair
The Honourable David Tkachuk

November 2003

Ce rapport est aussi disponible en français.
Des renseignements sur le Comité sont donnés sur le site:
www.senate-senat.ca/bancom.asp

Information regarding the Committee can be obtained through its web site:
www.senate-senat.ca/bancom.asp

DEBTORS AND CREDITORS SHARING THE BURDEN:

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Table of Contents

The Committee

The following Senators have participated in the study:

The Honourable Richard H. Kroft, C.M., Chair of the Committee
The Honourable David Tkachuk, Deputy Chair of the Committee

and

The Honourable Senators:

W. David Angus
Michel Biron, C.M.
D. Ross Fitzpatrick
Céline Hervieux-Payette, P.C.
James F. Kelleher, P.C.
E. Leo Kolber (past Chair of the Committee)
Paul J. Massicotte
Michael A. Meighen
Wilfred P. Moore
Donald H. Oliver
Marcel Prud'homme, P.C.
Raymond C. Setlakwe, C.M. (retired from the Senate on July 3, 2003)

Ex-officio members of the Committee:

The Honourable Senators: Sharon Carstairs, P.C. (or Fernand Robichaud, P.C.) and John Lynch-Staunton (or Noël A. Kinsella)

Other Senators who have participated from time to time on this study:

The Honourable Senators Maria Chaput, Leonard J. Gustafson, Pana Merchant and Madeleine Plamondon

Staff of the Committee:

Mr. Yoine Goldstein, Special Advisor to the Committee, Partner, Goldstein, Flanz & Fishman

Ms. June M. Dewetering, Acting Principal, Parliamentary Research Branch, Library of Parliament

Mr. Denis Robert, Clerk of the Committee, Committees and Private Legislation Directorate, The Senate

Mrs. Kelly J. Bourassa, Barrister and Solicitor, Policy Advisor to the Chair

Ms. Rhonda Walker, Policy Advisor to the Deputy Chair

Order of Reference

Extract from the *Journals of the Senate* of October 29, 2002:

"The Honourable Senator Kolber moved, seconded by the Honourable Senator Bacon:

That in accordance with the provisions contained in section 216 of the *Bankruptcy and Insolvency Act* and in section 22 of the *Companies' Creditors Arrangement Act*, the Standing Senate Committee on Banking, Trade and Commerce be authorized to examine and report on the administration and operation of the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act*; and

That the Committee submit its final report no later than June 19, 2003.

The question being put on the motion, it was adopted."

Extract from the *Journals of the Senate* of May 15, 2003:

"Resuming debate on the motion of the Honourable Senator Kolber, seconded by the Honourable Senator Rompkey, P.C.:

That the date for the presentation by the Standing Senate Committee on Banking, Trade and Commerce of the final report on its study on the administration and operation of the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act,* which was authorized by the Senate on October 29, 2002, be extended to Thursday, December 18, 2003.

After debate,

The question being put on the motion, it was adopted."

Paul Bélisle
Clerk of the Senate

Recommendations

Consumer Insolvency:

Federal Exempt Property:

1. The Bankruptcy and Insolvency Regulations be amended to provide a list of federal exempt property. The debtor should be required to choose, at the time of filing for bankruptcy and in its entirety, either the list of federal exempt property or the list of provincial/territorial exempt property available in his or her locality. The value of the property in the list of federal exempt property should be increased annually in accordance with increases in the cost of living as measured by the Consumer Price Index. (page 23)

Exemptions for RRSPs and RESPs:

2. The *Bankruptcy and Insolvency Act* be amended to exempt funds in all Registered Retirement Savings Plans from seizure in bankruptcy, provided that three conditions are met: the Registered Retirement Savings Plan is locked in; contributions made to the Registered Retirement Savings Plan in the one-year period prior to bankruptcy are paid to the trustee for distribution to creditors; and the exempt amount is no greater than a maximum amount to be set by regulation and increased annually in accordance with increases in the cost of living as measured by the Consumer Price Index. (page 29)

3. The *Bankruptcy and Insolvency Act* be amended to exempt funds in a Registered Education Savings Plan from seizure in bankruptcy, provided that two conditions are met: the Registered Education Savings Plan is locked in; and contributions made to the Registered Education Savings Plan in the one-year period prior to bankruptcy are paid to the trustee for distribution to creditors. (page 32)

Reaffirmation Agreements:

4. The *Bankruptcy and Insolvency Act* be amended to prohibit reaffirmation by conduct or by express agreement. (page 36)

Summary Administration:

5. The *Bankruptcy and Insolvency Act* be reviewed in order to eliminate all unnecessary procedural requirements and to provide parties to a bankruptcy with an opportunity – to the extent possible – to choose their level of involvement in accordance with a "by exception rather than by rule" approach. Moreover, the use of electronic communication should be encouraged in order to simplify and expedite the insolvency process. (page 39)

Non-Purchase Money Security Interests in Personal Exempt Property:

6. The *Bankruptcy and Insolvency Act* be amended to prohibit non-purchase money security interests in property that would otherwise be exempt from seizure in bankruptcy. Property should be defined to include exempted property intended for use or consumption by the debtor or the debtor's family, and should encompass apparel, household furnishings and motor vehicles owned by the debtor. (page 42)

Mandatory Counselling:

7. The *Bankruptcy and Insolvency Act* be amended to require the completion of mandatory counselling by first-time and second-time bankrupts as a condition of automatic discharge from bankruptcy available after 9 and 21 months respectively. Debtors making a consumer proposal should also undertake mandatory counselling. The nature and timing of mandatory counselling should be examined to ensure its effectiveness. (page 45)

Consumer Liens:

8. The issue of consumer liens continue to be addressed within provincial/territorial consumer protection legislation. (page 47)

Student Loans:

9. The *Bankruptcy and Insolvency Act* be amended to reduce, to five years following the conclusion of full- or part-time studies, the length of time prior to permitting the potential discharge of student loan debt. As well, the Act should allow the Court the discretion to confirm the discharge of all or a portion of student loan debt in a period of time shorter than five years where the debtor can establish that the burden of maintaining the liability for some or all of the student debt creates undue hardship. (page 56)

Discharge from Bankruptcy and the Treatment of Second-Time Bankrupts:

10. The *Bankruptcy and Insolvency Act* be amended to provide automatic discharge from bankruptcy after 21 months for second-time bankrupts who have completed mandatory counselling. The Superintendent of Bankruptcy, the trustee or any interested party should have the opportunity to oppose the automatic discharge, in the same way that the discharge of a first-time bankrupt can be opposed, thereby requiring a Court hearing. (page 59)

Contributions of Surplus Income to the Bankrupt's Estate:

11. The *Bankruptcy and Insolvency Act* be amended to require bankrupts with surplus income to contribute to their estate for a total of 21 months. Trustees should have the discretion to permit a shorter contribution period in cases of undue hardship. Surplus income should continue to be determined in accordance with the directive of the Superintendent of Bankruptcy. The discharge of the debtor should not be delayed merely because of the obligation to continue to contribute for a total of 21 months. In appropriate circumstances, a trustee should be able to seek a summary judgment to require such payments. (page 62)

Voluntary Agreements to Make Post-Discharge Payments:

12. The *Bankruptcy and Insolvency Act* be amended to allow trustees to enter into voluntary payment agreements with bankrupts who do not have surplus income. Fees payable to the

trustee in accordance with such an agreement should not exceed the minimum legal amount established for summary administration bankruptcies. (page 65)

Non-Dischargeable Credit Card Purchases:

13. The matter of purchases by the debtor of luxury or non-essential goods and services shortly prior to filing for bankruptcy continue to be decided either during the course of a discharge hearing or through an accusation of fraud. (page 67)

International Insolvency:

14. The *Bankruptcy and Insolvency Act* be amended to recognize the effect of a foreign discharge or compromise of debt with respect to an individual, provided certain conditions are met. The conditions should be: the bankrupt foreign-resident Canadian has a real and substantial connection with the foreign jurisdiction; the foreign procedure is fair and non-prejudicial to creditors; and the personal exemptions used by the bankrupt foreign-resident Canadian in the foreign proceedings are substantially similar to those in Canada. (page 70)

Debt Forgiveness by the Canada Customs and Revenue Agency:

15. The *Bankruptcy and Insolvency Act* be amended to provide that, for consumer proposals, the year-end date for income tax purposes is the date on which the proposal is filed with the Official Receiver. For commercial proposals, the year-end date should be the earlier of: the date of filing of the notice of intention to file a proposal; and the date of filing of the proposal with the Official Receiver. Moreover, the *Income Tax Act* should be amended to ensure that the debt forgiveness provisions in Section 80 of the Act are not applicable to individuals who file proposals under the *Bankruptcy and Insolvency Act*. (page 73)

Ipso Facto Clauses:

16. The *Bankruptcy and Insolvency Act* be amended to provide that *ipso facto* clauses in agreements for basic services are not enforceable with respect to consumer proposals and consumer bankruptcies. (page 75)

Credit Reporting:

17. The Office of the Superintendent of Bankruptcy take a leadership role in convening a meeting among credit granting agencies, credit grantors, provincial/territorial representatives and other relevant parties with a view to negotiating a mutually acceptable credit scoring regime. (page 79)

Inadvertent Discharge of Selected Claims in Proposals:

18. The *Bankruptcy and Insolvency Act* be amended to ensure that an insolvent debtor will not be released from the debts and liabilities referred to in Section 178 of the Act unless the holder of those debts provides affirmative and informed consent. (page 81)

Bankruptcy and Family Law:

19. The *Bankruptcy and Insolvency Act* be amended to:

- **ensure that bankruptcy does not prevent a claimant from recovering the total amount of support arrears from a bankrupt spouse;**
- **clarify that only Court orders made under Section 68 of the Act have priority over enforcement of spousal and child support against the bankrupt's income during the period of bankruptcy;**
- **provide that bankruptcy does not stay or release any claim for equalization or division against exempt assets under provincial/territorial legislation regarding equalization and/or the division of marital property;**

- **exclude, from assets vesting in the trustee, the right to sue the bankrupt's spouse for equalization or division of property under provincial/territorial matrimonial property law; and**

- **add, to the debts that survive bankruptcy, a debt for equalization or division of property under provincial/territorial matrimonial property law, to the extent that the debt arises from malicious or fraudulent dissipation or concealment of property by the bankrupt. (page 86)**

Commercial Insolvency:

Compensation Protection: Wages and Pensions:

20. The *Bankruptcy and Insolvency Act* be amended to provide that unpaid claims for wages and vacation pay arising as a result of an employer's bankruptcy be payable to an amount not to exceed the lesser of $2,000 or one pay period per employee claim. The funding of these claims should be assured by creating a super priority over secured claims to inventory and accounts receivable. The secured creditor or creditors should be able to assume the rights of the employees against the directors. (page 96)

21. The *Bankruptcy and Insolvency Act* not be amended to alter the treatment of pension claims. (page 99)

Debtor-in-Possession Financing:

22. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit Debtor-in-Possession financing. The Court should be given the jurisdiction to provide that the lien by the Debtor-in-Possession lender can rank prior to such other existing security interests as it may specify. As well, any secured creditor affected by such priority should be given notice of the Court hearing intended to authorize the creation of security ranking prior to its security. In deciding whether to authorize a Debtor-in-Possession loan, the Court should be required to consider the seven factors outlined by the Joint Task Force on Business Insolvency Law Reform in its March 2002 report. (page 103)

The Rights of Unpaid Suppliers:

23. The *Bankruptcy and Insolvency Act* be amended to repeal, subject to the noted exception, the provisions that provide protection for unpaid suppliers of goods to bankrupt companies.

The provisions that protect the rights of farmers, fishers and aquaculturalists as suppliers should be retained. (page 111)

Cross-Border Insolvencies:

24. The *Bankruptcy and Insolvency Act* be amended to incorporate the United Nations Commission on International Trade Law Model Law on Cross-Border Insolvency. Consideration should be given to adding a reciprocity provision and provisions that would assure the creation of a creditors' committee, consisting of Canadian creditors, to protect their interests. The reasonable expenses of the members of this committee should be paid by the foreign debtor, if considered appropriate by the Canadian Court. (page 117)

Director Liability:

25. The *Bankruptcy and Insolvency Act* be amended to include a generally applicable due diligence defence against personal liability for directors. (page 120)

Transfers at Undervalue and Preferences:

26. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to ensure consistent and simplified rules for challenging fraudulent preferences, conveyances at undervalue and other reviewable transactions. A trustee/monitor under a proposal should have the same powers as a trustee in bankruptcy. The Acts should provide a standard for challenging transactions that may affect the value of creditors' realizable claims. (page 123)

Bankruptcies by Securities Firms:

27. The *Bankruptcy and Insolvency Act* be amended to clarify: the definition of "net equity;" the status of cash in the accounts of bankrupt securities firms; and the applicability of Part XII of the Act to electronic transactions. (page 125)

Financial Market Issues:

28. The *Companies' Creditors Arrangement Act* be amended to give the Court the right to exempt securities regulators from Court-ordered stays of proceedings in instances where two conditions are met: the exemption is needed for the protection of third parties; and the exemption does not subject directors or senior management to undue pressure and loss of time. (page 127)

Insolvency Practitioner Liability as a Successor Employer:

29. The *Bankruptcy and Insolvency Act* be amended to separate clearly the personal liability of an insolvency practitioner from the liability of the debtors' estate. (page 130)

Executory Contracts:

30. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit disclaimer of executory contracts in existence on the date of commencement of proceedings under the Acts. This disclaimer should apply to all executory contracts, provided a number of conditions are met. In particular: the debtor should be obliged to establish inability or serious hardship in restructuring the enterprise without the disclaimer; the co-contracting party should be permitted to file a claim in damages in the restructuring; and, where a collective agreement is being disclaimed, the debtor should also have the burden of establishing that post-filing negotiations have been carried on, in good faith, for relief of too onerous aspects of the collective agreement and should establish in Court that the disclaimer is necessary in order to allow for a viable restructuring. (page 137)

31. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit trustees, Court-appointed receivers and monitors, if authorized by judgment, to assign executory contracts when appropriate, in connection with going concern transactions and on a liquidation basis, provided that two conditions are met: the proposed assignee is at least as

credit worthy as the debtor was at the time the contract was entered into; and the proposed assignee agrees to compensate the other party for pecuniary loss resulting from the default by the debtor or give adequate assurance of prompt compensation. (page 138)

Workers' Compensation Board Premiums:

32. The *Bankruptcy and Insolvency Act* be amended to return the treatment of Workers' Compensation Board premiums to that which existed prior to 1997. (page 143)

Interim Receivers:

33. The *Bankruptcy and Insolvency Act* be amended to clarify the role of the interim receiver, and the duration and meaning of the term "interim." As well, the definition of "receiver" should be amended to include interim receivers when they operate in a manner similar to Court-appointed receivers. (page 145)

Going Concern and Asset Sales:

34. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit the debtor, subject to prior approval of the Court, to sell part or all of its assets out of the ordinary course of business, during reorganization and without complying with bulk sales legislation. Similarly, the debtor should be permitted to sell all or substantially all of its assets on a going concern basis. On an application for permission to sell, the Court should take into consideration whether the sales process was conducted in a fair and reasonable manner and whether major creditors were given reasonable notice, in the circumstances, of the proposed sale and had input into the decision to sell. No such sale to controlling shareholders, directors, officers or senior management of the debtor having a significant financial interest in the purchaser or in the sales transaction should be permitted, other than in exceptional circumstances. (page 148)

Governance:

35. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit the Court to replace some or all of the debtor's directors during proposals or reorganizations if the governance structure is impairing the process of developing and implementing a going concern solution. Moreover, prior to appointment, a trustee/monitor should disclose, to the Court, any business and legal relationships it has or has had with the debtor. The auditor or recent former auditor of the debtor should not be permitted to be the monitor. Furthermore, the monitor should not be permitted, in the event of a failed restructuring, to become the trustee or a receiver for a secured creditor. (page 150)

Plan Approvals:

36. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to require a trustee/monitor to provide, in connection with a request for Court approval of a reorganization plan, an opinion that, as a group, each of secured creditors and unsecured creditors are likely to receive no less under the plan than it would receive in a liquidation. Moreover, Section 54(3) of the *Bankruptcy and Insolvency Act* regarding related parties should be incorporated in the *Companies' Creditors Arrangement Act*. Finally, the Acts should be amended to provide the Court approving a reorganization plan with the power to approve a restructuring of the equity of the debtor, with or without shareholder approval. (page 152)

Priorities:

37. The *Companies' Creditors Arrangement Act* be amended to incorporate the priority rules in the *Bankruptcy and Insolvency Act*. (page 153)

Insolvency of Other Vehicles:

38. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to provide for the liquidation or the reorganization of a business trust. (page 155)

Income Tax:

39. The *Income Tax Act* be amended to provide that distress preferred share treatment for tax purposes be afforded to qualifying debt, for a specified period of time, by filing a notice of election with the Canada Customs and Revenue Agency. Moreover, on the consummation of a plan of arrangement, a debtor should be able to elect to use fresh start accounting for tax purposes, with tax obligations relating to the period prior to the date of bankruptcy addressed as pre-filing claims. (page 157)

Subordination of Equity Claims:

40. The *Bankruptcy and Insolvency Act* be amended to provide that the claim of a seller or purchaser of equity securities, seeking damages or rescission in connection with the transaction, be subordinated to the claims of ordinary creditors. Moreover, these claims should not participate in the proceeds of a restructuring or bankruptcy until other creditors of the debtor have been paid in full. (page 159)

Administrative Tribunals and Stays of Proceedings:

41. The *Companies' Creditors Arrangement Act* be amended to exempt, from the application of stays of proceedings and subject to Court discretion, all proceedings brought before non-judicial administrative tribunals. The exemption should be granted where two conditions are met: the exemption is needed for the protection of third parties; and the exemption does not subject directors or senior management to undue pressure and loss of time. (page 162)

Administrative and Procedural Issues:

Volume of Filings, Access to the Process and Funding of the Office of the Superintendent of Bankruptcy:

42. The *Bankruptcy and Insolvency Act* be reviewed in order to identify opportunities that will contribute to greater efficiency within the insolvency system, including efforts regarding the adoption of new technologies. (page 167)

43. The *Bankruptcy and Insolvency Act* be amended to provide the Superintendent of Bankruptcy with the authority to finance research and education programs from the account which contains unclaimed dividends and undistributed funds. Amounts that are unclaimed or undistributed after a two-year period should be used in this way. (page 169)

Consolidation of Insolvency Statutes:

44. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* continue to exist as separate statutes. (page 173)

Statutory Review of Insolvency Legislation:

45. The *Bankruptcy and Insolvency Act*, the *Companies' Creditors Arrangement Act*, the *Winding-Up and Restructuring Act* and the *Farm Debt Mediation Act* be amended to require a review by a Parliamentary committee at least once every five years. (page 176)

A Specialized Judiciary:

46. The federal government consult with relevant stakeholders with a view to developing education and training programs that

would enable judges in Canada to develop specialized expertise in the area of insolvency law. (page 180)

Issues of Costs:

47. The *Bankruptcy and Insolvency Act* be amended to repeal the Tariff of Costs. Instead, costs should be paid in accordance with civil Court tariffs as they apply from place to place throughout Canada. (page 183)

Conflicts of Interest:

48. The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be reviewed in order to identify and eliminate any opportunities for the roles and responsibilities of insolvency practitioners to place them in a real or perceived conflict of interest. Moreover, in order to ensure that all practitioners fulfill their duties with a high level of integrity, the federal government should adopt guidelines for insolvency practitioners regarding professional conduct and conflicts of interest, expanding upon Rules 34 to 53 of the *Bankruptcy and Insolvency Act* where appropriate. (page 185)

The Definition of Income:

49. The *Bankruptcy and Insolvency Act* be amended in order to clarify the meaning of the term "total income." As well, clarity – in the form of guidelines contained in a directive of the Superintendent of Bankruptcy – should be provided to trustees regarding the manner in which lump-sum settlements received after bankruptcy and before discharge should be divided between debtors and creditors. Finally, a bankrupt's tax refunds received during a period to be determined by statute should be made available to the trustee for distribution to creditors. (page 189)

The Definition of Consumer Debtor:

50. The *Bankruptcy and Insolvency Act* be amended to raise the indebtedness threshold contained in the definition of "consumer

debtor" to $100,000, with annual increases thereafter to reflect increases in the cost of living as measured by the Consumer Price Index. Moreover, two years after the new indebtedness threshold comes into force, the federal government should initiate a review of the degree to which insolvent debtors are using the consumer proposal option rather than pursuing a commercial reorganization. (page 190)

Selection of the Bankruptcy Trustee:

51. The *Bankruptcy and Insolvency Act* be amended to provide that the debtor is required to submit to the Official Receiver his or her choice of a trustee to administer his or her bankruptcy. (page 193)

Non-Arm's Length Creditor Voting Rights:

52. The *Bankruptcy and Insolvency Act* be amended to provide voting rights to non-arm's length creditors who have been dealing with the debtor at non-arm's length in the year prior to the bankruptcy, if they represent together more than 40% of the value of the total claims. In the event that the non-arm's length creditors vote changes the outcome of the vote, any interested party should then seek leave of the Court to have the vote included. (page 196)

Debts Not Released by an Order of Discharge:

53. The *Bankruptcy and Insolvency Act* be amended to require that fraud be proven in order for a debt to survive discharge from bankruptcy. Moreover, the provisions should apply to both debts for property and debts for services acquired through false pretences or fraudulent misrepresentation. (page 198)

Acknowledgements

I would like to express my personal thanks to the members of the committee who were available for many extended meetings in order to hear the evidence of all of the witnesses who appeared before us over the course of our study. Additionally, I would like to thank all of the witnesses who appeared before us, representing the various stakeholder groups. The quality of the evidence presented to us, both orally and in written submissions, and the ability of the witnesses before the committee to respond, on short notice, to often complex questions demonstrated their expertise and dedication to improving Canada's bankruptcy and insolvency laws. They were of great assistance to the committee in completing such a lengthy study in a very short period of time.

Particular mention must be given to the Parliamentary Research Branch of the Library of Parliament and, in particular, the researcher for our committee, Ms. June Dewetering. June's work in assisting the committee to complete this report has been outstanding. I would also like to thank the Clerk of the Committee, Denis Robert, Senate support staff and translators who assisted the committee in completing this study in a very short time frame. The result is a review of Canadian insolvency legislation, and particularly the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act, that the committee hopes will be helpful to the federal government in drafting much needed legislation. Counsel for the committee, Mr. Yoine Goldstein, provided enormous assistance to the committee in addressing all of the many areas that required consideration and in advising the committee with respect to those areas of review that were particularly technical. It is no exaggeration to say that we could not have completed our work in the time and the way that we have without the benefit of his wisdom, experience and commitment.

I know I speak on behalf of our entire committee in saying; it is our sincere hope that the government will lose no time in acting to implement amended legislation in these areas. We look forward to our opportunity to review such legislation when it reaches the Senate for review.

Richard H. Kroft

Chair, Standing Senate Committee on Banking, Trade and Commerce

DEBTORS AND CREDITORS SHARING THE BURDEN: A REVIEW OF THE *BANKRUPTCY AND INSOLVENCY ACT* AND THE *COMPANIES' CREDITORS ARRANGEMENT ACT*

CHAPTER ONE: INTRODUCTION

Canada has a long history of insolvency legislation, beginning in 1869 with *An Act Respecting Insolvency*, which covered voluntary and compulsory bankruptcies, provided for compositions and applied only to traders. This legislation was followed by the *Insolvent Act of 1875*, which was repealed in 1880. For the next four decades, until the passage of the *Bankruptcy Act* in 1919, Canada lacked bankruptcy legislation of uniform application across the nation. Since then, Canadian bankruptcy legislation has been amended in a substantive manner in 1949, 1992 and 1997.

Furthermore, although not used frequently until the 1980s, the *Companies' Creditors Arrangement Act* (CCAA) became law in 1933, with amendments made in 1997. The third pillar of insolvency legislation, the *Winding-up and Restructuring Act*, was passed in 1882. A fourth statute, the 1997 *Farm Debt Mediation Act,* was passed as the successor to the 1986 *Farm Debt Review Act*, and applies to the farming industry.

Numerous attempts have been made in the last three decades to amend Canada's bankruptcy and insolvency laws …

Numerous attempts have been made in the last three decades to amend Canada's bankruptcy and insolvency laws, and although six omnibus reform bills were introduced in Parliament between 1975 and 1984, none of the proposals became law. Moreover, during that period, a number of advisory committees examined various aspects of the laws and made recommendations for change. In view of the relative lack of success with omnibus legislation, however, a strategic decision was made to propose amendments in selected areas.

Consequently, in June 1991, Bill C-22 was introduced in the House of Commons. The Bill, which came into force in November 1992, contained a provision requiring review of the *Bankruptcy and Insolvency Act* (BIA) by a Parliamentary committee three years after coming into force. With a statutory Parliamentary review required in 1995, Industry Canada – then the Department of Consumer and Corporate Affairs – established the Bankruptcy and Insolvency Advisory Committee, with several working groups and task forces comprised of public and private sector representatives.

Designed as a forum in which priorities for reform to bankruptcy and insolvency laws could be discussed and in which consensus on policy recommendations might be reached, the Bankruptcy and Insolvency Advisory Committee made a number of recommendations that found legislative expression in Bill C-5, which was originally introduced in the first session of the Thirty-Fifth Parliament as Bill C-109.

Bill C-5 was introduced in the House of Commons in March 1996. The Bill proposed to amend the BIA with respect to: the licensing and regulation of bankruptcy trustees; the liability of trustees for environmental damage and claims; liability of directors and stays of action against directors during reorganizations; compensation for landlords where leases are disclaimed in a proposal under the BIA; procedures in consumer proposals; consumer bankruptcies; the dischargeability of student loan debt; Workers' Compensation Board claims; a requirement for bankrupts to contribute part of their income to the bankruptcy estate; international insolvencies; and securities firm insolvencies. The Bill also proposed amendments to the CCAA in order to align more closely the provisions of the CCAA and the BIA. Beginning in November 1996, the Standing Senate Committee on Banking, Trade and Commerce reviewed Bill C-5, and recommended amendments that were adopted by the Senate and, subsequently, the House of Commons before the Bill received Royal Assent in April 1997.

Anticipating a five-year statutory Parliamentary review of the BIA and the CCAA, as required by Bill C-5, in 2001

and 2002 Industry Canada held consultations with stakeholders on a range of insolvency issues. Consumer insolvency concerns were also examined by the Personal Insolvency Task Force, an independent panel established in 2000 by the Office of the Superintendent of Bankruptcy with membership from the principal stakeholder groups.

The Personal Insolvency Task Force released its report in August 2002, while Industry Canada published its *Report on the Operation and Administration of the* Bankruptcy and Insolvency Act *and the* Companies' Creditors Arrangement Act in September 2002. A third insolvency statute – the *Winding-up and Restructuring Act* – is not subject to the current statutory Parliamentary review; nor is the fourth law, the *Farm Debt Mediation Act*.

With the knowledge gained through examination of previous amendments to the BIA and the CCAA, in May 2003 the Standing Senate Committee on Banking, Trade and Commerce began a review of the *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* with a view to determining whether the legislation, as it is currently written, is meeting the needs of the full range of stakeholders: debtors, creditors, judges, lawyers, trustees and other insolvency practitioners, the Office of the Superintendent of Bankruptcy and – importantly – all Canadians through the impact of insolvency laws on our economy.

In the course of the Committee's study, we have heard from a wide range of groups and individuals: … . They have shared their invaluable insights about this enormously complex area: what is working, what is not, and how they think the BIA and the CCAA should be changed.

In the course of the Committee's study, we have heard from a wide range of groups and individuals: academics, a variety of practitioners, credit counsellors, labour unions, business groups and others. They have shared their invaluable insights about this enormously complex area: what is working, what is not, and how they think the BIA and the CCAA should be changed.

This report comments on the Committee's philosophy regarding the fundamental principles that should guide the design of insolvency laws in Canada, with particular reference to the two statutes that are the subject of this review: the BIA and the CCAA. It also discusses the socio-economic importance of insolvency legislation, and describes the magnitude and nature of the insolvency problem in Canada. Most importantly, the testimony presented to the Committee by witnesses, as well as

[W]e believe that the ideas [contained in Chapters 4 and 5 of the Personal Insolvency Task Force's Report] have merit – particularly from the perspective of streamlining the process and of reducing costs – …

our recommendations for changes to the statutes and conclusions reached, are highlighted.

Although no discussion or recommendations occur with respect to the procedural changes regarding consumer bankruptcies and proposals identified by the Personal Insolvency Task Force in Chapters 4 and 5 of its report, we believe that the ideas have merit – particularly from the perspective of streamlining the process and of reducing costs – and urge relevant stakeholders to engage in the discussions needed to achieve consensus about how they should be addressed in future amendments to our insolvency legislation.

Finally, a number of Appendices provide relevant background information. Appendix A summarizes the key elements of the *Winding-up and Restructuring Act* and the *Farm Debt Mediation Act*, which are not part of the Committee's current review, while Appendix B notes changes over time to Canada's main insolvency laws – the BIA and the CCAA – and provides a general discussion of how the insolvency process works for consumers and corporations. Appendix C summarizes the report published by Industry Canada following its consultations with stakeholders on administrative policy, commercial insolvency and consumer insolvency issues, and Appendix D concludes with brief details on selected aspects of insolvency legislation in other countries.

CHAPTER TWO:
THE COMMITTEE'S PHILOSOPHY WITH RESPECT TO INSOLVENCY LAW

As the Committee began this study, we focussed on what we believe should be the fundamental principles guiding the design of insolvency laws in this country. Certain prerequisites for a well-functioning insolvency system continually struck us as important: fairness, accessibility, predictability, responsibility, cooperation, efficiency and effectiveness. These are all critical hallmarks to remember as legislative changes are proposed.

Certain prerequisites for a well-functioning insolvency system continually struck us as important: fairness, accessibility, predictability, responsibility, cooperation, efficiency and effectiveness. These are all critical hallmarks to remember as legislative changes are proposed.

Canada's insolvency system must be – and must be perceived to be – fair. Fairness is an essential consideration not only for Canadians, but also for residents of other countries. It must be fair for debtors, who should be provided with tools to avoid bankruptcy if that is the best option or with a true "fresh start" when they are discharged from their bankruptcy, and for creditors, who extend credit with the expectation of full repayment on a timely basis or, when this circumstance does not occur, are provided with a predictable, fair and orderly means by which loss is both shared appropriately and minimized to the extent possible.

Moreover, it must be fair for judges, who should have both clear rules to guide their decision making and the flexibility needed to address the unique circumstances of each case, and for trustees, monitors and other insolvency practitioners, who also require comprehensive guidelines about their rights and responsibilities. It must also be fair for foreign entities, who may find themselves involved in a cross-border insolvency, and for Canadians more generally, who need a fair, predictable system that provides stakeholders with incentives to act with integrity and transparency in order that our economic system remains sound and facilitates prosperity for all.

The redistributive effects of bankruptcy must be considered from the perspective of fairness, since bankruptcy-related losses for creditors may lead to higher costs of credit for those who pay their debts fully and in a timely manner. In some sense, fairness would dictate that the burden faced by those who

pay their debts must not be too great because of the actions and omissions of those who do not.

… the Committee believes that the insolvency system must be accessible to debtors – with any level of debt and in all regions of Canada – as a right, not a privilege.

As well, the Committee believes that the insolvency system must be accessible to debtors – with any level of debt and in all regions of Canada – as a right, not a privilege. In order for the system to be meaningful, it must also be accessible from the perspective of being easily understood by stakeholders. It should be, at least to some extent, flexible. Each situation of insolvency is different, and while uniformity and predictability generally are critically important, some flexibility is also needed so that judges can make the decisions required in the best interest of all stakeholders.

The Committee also believes that Canadian insolvency laws must be drafted in a manner that ensures a high level of predictability for all stakeholders, domestic and international. Everyone should have a clear understanding of how the insolvency process operates and the options that are available; consistency should enable the likely outcomes to be predicted with a relatively high degree of accuracy. Predictability will enable stakeholders to make the best possible choices given their particular circumstances: debtors to decide between bankruptcy and a consumer proposal or commercial reorganization, suppliers and creditors to assess the likely outcome of debtor default as a contributing factor in their decision about whether to supply and extend credit and at what cost, domestic and foreign investors about whether to make an investment, and judges to determine the most appropriate orders to be made and actions to be taken in particular circumstances, among others.

Canada's insolvency system must also be characterized by responsible behaviour and cooperation. Recognizing that insolvency often occurs for reasons unrelated to financial mismanagement, the system must provide incentives for debtors to behave responsibly in managing their finances and for creditors to act likewise in their granting of credit. Trustees and other insolvency practitioners must also fulfill their responsibilities in a conscientious manner. There must be

meaningful consequences for any party that fails to act in accordance with the law.

The parties must also be provided with the incentives needed to ensure that they act cooperatively, since cooperation is also a prerequisite for a well-functioning insolvency system: cooperation among debtors and their creditors as they attempt to negotiate a mutually acceptable restructuring arrangement, among the Court, debtors and creditors as reorganization plans are finalized, and among trustees, debtors and creditors as bankruptcy estates are administered. Canada's insolvency system is highly regarded internationally, in part because of its emphasis on cooperation.

The Committee feels, as well, that our insolvency system must be efficient and effective. It must consider the social and economic costs of bankruptcy and ensure that these costs are minimized and shared appropriately. Moreover, situations of insolvency must be resolved with the least possible cost to stakeholders; every action taken by trustees, monitors and others must have a useful purpose. The system must also facilitate the efficient reallocation of resources in the event of bankruptcy, incorporate incentives for proper behaviour by all stakeholders and meet the needs of all stakeholders in an ever-changing environment.

A fundamental issue underlying insolvency is that there are inadequate resources available to satisfy everyone and the situation is a zero-sum game: a fresh start for a bankrupt means that creditors do not fully recover the moneys owed to them, and the greater the share of assets allocated to any particular creditor or class of creditors, the smaller is the share of assets available for distribution to all other creditors or classes of creditors.

Throughout our hearings, the Committee was mindful that the emphasis in Canada has been on finding the proper balance between providing debtors with unmanageable debt with a reasonable opportunity to make a financial recovery or to have a "fresh start" following discharge from their bankruptcy and ensuring that creditors, to the extent possible, share the burden of loss appropriately. A fundamental issue underlying insolvency is that there are inadequate resources available to satisfy everyone and the situation is a zero-sum game: a fresh start for a bankrupt means that creditors do not fully recover the moneys owed to them, and the greater the share of assets allocated to any particular creditor or class of creditors, the smaller is the share of assets available for distribution to all other creditors or classes of creditors.

The Committee considers that in a society such as ours, and particularly as globalization continues, risk-taking behaviour

contributes to success in a market-based economy; it is this behaviour that will help to ensure our prosperity as a nation and our place globally. Risk-taking behaviour, however, inevitably carries with it some failures. Data illustrating the extent to which the self-employed and small businesses experience financial difficulties show this fact to be true. If we, as a society, support risk-taking behaviour because of the prosperity it brings, then we, as a society, must also be willing to bear the cost of failures – within reason – and to forgive instances where the taking of risks has a negative outcome.

If we, as a society, support risk-taking behaviour because of the prosperity it brings, then we, as a society, must also be willing to bear the cost of failures – within reason – and to forgive instances where the taking of risks has a negative outcome.

From this perspective, the manner in which a country addresses insolvency is tied to other decisions: about support for entrepreneurial behaviour as an engine of growth, about the promotion of education as a contributor to the well-educated workforce needed for the future, and about the extent to which safety nets are provided by governments to assist those who are less fortunate, among others. In this sense, a country's insolvency laws are framework legislation. They are a key indicator of how a country governs itself, its businesses and its citizens, and about its priorities for its future. These laws are also among those thought to be important for nations that participate in the global economy, since they regulate certain aspects of international commerce and are considered by those wishing to invest in Canada and make multinational corporate decisions.

The Committee has given consideration to the proper sharing of the burden of loss between debtors and creditors. We want a discharged bankrupt to have the best possible chance for future success and for a meaningful contribution to our economy and to our society. We also want to ensure, however, that due consideration is given to how the treatment of debtors affects others, including creditors, those who pay their debts in full and on time, and the Canadian economy more generally. In developing our recommendations, we continuously reflected on the extent to which our proposals would ensure that the fundamental principles of fairness, accessibility, predictability, responsibility, cooperation, efficiency and effectiveness are respected. We believe that our recommendations strike the appropriate balance.

CHAPTER THREE:
INSOLVENCY LEGISLATION AND WHY IT IS NEEDED

A. The Socio-Economic Importance of Insolvency Laws

Bankruptcy and insolvency situations usually have devastating effects for everyone affected: the consumer or corporate debtor, family and friends, communities, unpaid suppliers, uncompensated – and perhaps unemployed – employees, creditors and shareholders, among others. A debtor's financial difficulties generally mean that shareholders lose value, unpaid suppliers and creditors may themselves face insolvency or bankruptcy, uncompensated employees may experience personal insolvency or bankruptcy, communities – particularly if they are small, have a single industry, and involve a number of affected suppliers and employees – probably will not thrive, even if they do survive, and governments at all levels potentially lose tax revenues as a consequence of reduced economic activity yet may face higher costs for employment insurance and social assistance.

Bankruptcy and insolvency situations usually have devastating effects for everyone affected: the consumer or corporate debtor, family and friends, communities, unpaid suppliers, uncompensated – and perhaps unemployed – employees, creditors and shareholders, among others.

In essence, insolvency laws exist in order to provide:

- debtors with an opportunity to obtain a discharge from their debts, subject to conditions, and thereby become productive and useful citizens free from an unsustainable debt burden, in essence to get a fresh start;
- a relatively quick, inexpensive method by which insolvent debtors can be compelled to give their non-exempt property to a trustee with a view to realizing these assets for the benefit of creditors;
- a mechanism for the orderly distribution of the non-exempt property of insolvent debtors among their creditors in order that the burden is shared appropriately;

- an opportunity to investigate the affairs of bankrupts and to reverse any improper transactions that occurred prior to bankruptcy; and
- a framework within which the financial obligations of debtors can be compromised or restructured in order to avoid bankruptcy.

Canada's insolvency laws fundamentally contribute to the effective and efficient functioning of the marketplace, since their existence gives some security to all stakeholders, domestic and foreign. From a financial perspective alone, the fairness and predictability provided by these laws increase the amount of credit that is available and help to ensure that it is available at reasonable cost. In turn, the availability of credit at reasonable cost has implications for the levels of domestic and foreign investment, entrepreneurship and innovation, and personal investment and consumption.

… with an increased focus on global competitiveness, Canada's insolvency laws must be – and must be seen to be – effective and fair, and amendments to the laws must be made with efficiency and predictability in mind.

In the event of financial difficulty, the timeliness, transparency and fairness with which assets can be redeployed to more productive and profitable uses affects economic performance and minimizes losses for creditors. Moreover, with an increased focus on global competitiveness, Canada's insolvency laws must be – and must be seen to be – effective and fair, and amendments to the laws must be made with efficiency and predictability in mind.

Of Canada's insolvency laws – the *Bankruptcy and Insolvency Act*, the *Companies' Creditors Arrangement Act*, the *Winding-up and Restructuring Act* and the *Farm Debt Mediation Act* – the two most important are the *Bankruptcy and Insolvency Act* (BIA) and the *Companies' Creditors Arrangement Act* (CCAA). The BIA applies to individuals and companies with unsustainable debt burdens, while companies can reorganize under either statute in the event of financial difficulty provided a $5 million debt threshold is met with respect to the CCAA. The third statute – the *Winding-up and Restructuring Act* – is primarily used in situations involving financial institutions, while the fourth – the *Farm Debt Mediation Act* – applies to insolvent farmers; these latter two Acts are not part of the Committee's current review.

B. The Magnitude and Nature of the Problem

In developing an insolvency regime that is appropriate to the magnitude and nature of the insolvency problem, some consideration must be given to the circumstances giving rise to insolvency and its recurrence. The preferred option must surely be an identification of the reasons for insolvency, in order that preventive measures can be developed to assist consumers and corporations in avoiding financial difficulties. The public interest is thereby served.

The preferred option must surely be an identification of the reasons for insolvency, in order that preventive measures can be developed to assist consumers and corporations in avoiding financial difficulties.

In general, financial difficulties might occur for a number of economic and non-economic reasons, bearing in mind that non-economic reasons frequently have economic consequences. Studies have revealed the following factors as contributors to insolvency: unemployment; underemployment; retirement; compulsive spending; a change in marital, family or health status; substance addiction; gambling; loss of corporate market share; bad weather; international trade sanctions; and business failure which may cause personal insolvency. While also a potential cause of insolvency, financial mismanagement might more often be a contributing factor where one or more other factors also exist.

Individuals and corporations most often cannot control economic circumstances, while non-economic factors may be only partially controllable. Nevertheless, most agree that financial counselling designed to help individuals and businesses assess their attitudes and beliefs regarding credit and its uses, acquire money management and budgeting skills, and identify warning signs associated with financial difficulty are useful. This type of counselling, however, is perhaps most effective before financial difficulties occur. It is for this reason that many advocate money management and budget skills as a skill area that should be taught to high school students.

While some believe that the increased availability of reasonably priced credit is to blame for financial difficulties, it is perhaps more useful to examine the extent to which

consumer bankruptcies have been rising while the aggregate amount of consumer credit as a proportion of disposable income has been relatively stable.

The magnitude and nature of insolvency problems among Canadians and Canadian businesses have varied over time, largely in response to changing economic conditions, but perhaps also because the stigma of bankruptcy appears to have lessened somewhat. As well, in a society where credit is important and readily available, a certain number of bankruptcies might be seen as a logical and inevitable consequence of credit availability.

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Studies reveal that, for some Canadians, their personal debt more than exceeds their annual disposable income. At present, the ratio of personal debt to annual disposable income exceeds 100%, an increase from 61% two decades earlier. The level of consumer indebtedness is thought to have risen by more than 238% over the 1981 to 2001 period, from $262.4 billion ($1997) in 1981 to $625.6 billion in 2001. The changing debt-to-income ratio could reflect changing attitudes by debtors and creditors to risk, a more tolerant attitude toward bankruptcy and/or a reduced stigma associated with bankruptcy.

Over the 1966 to 2002 period, insolvency cases filed with the Office of the Superintendent of Bankruptcy (OSB) increased, on average, by 8.8% annually, although the highest annual average rates of increase occurred in the 1970s; since 1997 the rate has been 1.1%. There are relatively significant differences between the average rate of increase in commercial and in consumer insolvencies filed with the OSB.

Over the 1966 to 2002 period, the average annual rate of increase in consumer insolvencies was 11.4%, and in 2001 there were almost 93,000 consumer insolvencies or 2.98 per 1,000 Canadians. The average annual rate of increase in consumer insolvencies reached 22.6% in the 1970s before falling to about 7.5% in the 1980s and 1990s. Over the 1997

to 2002 period, the average annual rate of increase in consumer insolvencies was markedly lower, at 2.0%.

Since 1999, the number of consumer bankruptcies filed with the OSB has been rising, although consumer proposals are increasingly popular with debtors as a means of avoiding bankruptcy and protecting certain assets, such as their homes. The 1993 to 2002 period has seen a continuous increase in the number of consumer proposals filed with the OSB; the number of such proposals has increased from about 1,900 in 1993 to more than 15,200 in 2002, which represents an average annual increase of 25.9% over the period.

The average annual rate of increase in corporate insolvencies was 3.6% over the 1966 to 2002 period, about one-third the rate of increase in consumer insolvencies. The average annual rate of increase reached 8.0% in the 1970s and 6.0% in the 1980s before falling to –0.6% in the 1990s. The average annual rate of increase declined further to –4.7% over the 1997-2002 period, and reached –7.6% for 2001-2002.

Corporate proposals have also been popular over the 1993 to 2002 period; during this time, the number of these proposals has increased, on average, 14% annually. Since the mid-1970s, the majority of the Office of Superintendent of Bankruptcy's cases have been consumer insolvencies, and in 2002 corporate insolvencies represented 10% of all cases addressed by the OSB.

Ontario and Quebec have the largest number of insolvency cases filed with the OSB each year, both by consumers and by corporations. This fact is not surprising given their population size and the number of businesses operating there.

In 2002, the Atlantic region, Quebec and Alberta exceeded the national average in terms of consumer insolvencies per 1,000 residents aged 18 years and over, while Ontario, Manitoba/Saskatchewan and British Columbia were

below the national average. In that year, the national average was 3.8 per 1,000 residents aged 18 years and over.

In 2002, corporate insolvencies per 1,000 businesses exceeded the national average in the Atlantic region, Quebec and Alberta; the rate in Ontario, Manitoba/Saskatchewan and British Columbia was lower than the national average. In that year, the national average was 5.9 per 1,000 businesses. In 2002, most corporate insolvency cases arose in the services and wholesale/retail trade sectors; the lowest number of cases occurred in the finance, insurance and real estate, manufacturing and primary sectors.

The regional pattern is, therefore, consistent for both consumer and corporate insolvencies when population and business distribution are considered.

… the level and depth of insolvency and economic prosperity are linked.

As noted above, the level and depth of insolvency and economic prosperity are linked. In 1992, the percentage of declared liabilities in insolvencies reached 1.75% of Gross Domestic Product. Although this percentage declined until 1999, since that time it has risen, reaching 1.5% in 2002. The increase is largely the consequence of corporate liabilities.

C. The *Bankruptcy and Insolvency Act*

Canada's *Bankruptcy and Insolvency Act*, which applies to commercial and consumer – or corporate and personal – insolvencies, provides a number of options for debtors who find themselves with an unsustainable debt burden, including bankruptcy in either case, and proposals for consumers and reorganizations for commercial enterprises, depending on the debtor's degree of financial difficulty.

Consumers and corporations who are in financial difficulty may make a proposal to their creditors – a "consumer proposal" or a "reorganization," as the case may be – to restructure their debt. This restructuring generally involves the acceptance of partial payment in fulfillment of debt and/or payments over a longer period of time. With this option, debtors retain control of their assets and creditors generally recover a greater amount; the consumer or corporation can continue to function and, hopefully, return to financial viability. Creditors generally have an incentive to agree to a proposal or reorganization if they expect that a greater return could be realized than if the consumer or corporation were to become bankrupt.

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To be eligible to make a consumer proposal, an individual's debts cannot exceed $75,000, excluding the mortgage on a principal residence, and he or she must have adequate resources to enable the development of a fair and realistic proposal. Consumer proposals are not binding on secured creditors; these creditors retain their right to realize on their security if timely payments are not made. Commercial proposals can be filed regardless of the amount of indebtedness, and secured creditors are similarly able to realize on their security if timely payments are not made.

The BIA contains incentives that encourage insolvent debtors to make a proposal rather than pursue bankruptcy. For example, some consumer bankrupts are required to make surplus income payments to their estate, which provides less

flexibility than a consumer proposal that provides the debtor with more flexibility regarding payments. Moreover, the trustee is required to report – prior to discharge from bankruptcy being granted – whether the debtor could have made a feasible consumer proposal; if so, the Court may grant a conditional discharge and the conditions imposed may resemble the payment arrangements in a proposal.

Where there is no reasonable hope of returning to financial viability, insolvent consumers and corporations may declare bankruptcy. Alternatively, creditors may request that insolvent consumers or corporations be placed in bankruptcy. In situations of bankruptcy, the process serves a number of functions:

- it provides a mechanism for liquidating the debtor's assets for the benefit of creditors;
- it enables the debtor to start over without the burden of unsustainable debt; and
- it allows assets to be re-allocated for use in an environment where profitability may exist.

The BIA, with its structured system for consumer proposals, corporate reorganizations, and bankruptcies, is thought to ensure a relatively predictable and consistent outcome.

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D. The *Companies' Creditors Arrangement Act*

Corporate reorganizations that involve in excess of $5 million in debt can occur under either the BIA or the *Companies' Creditors Arrangement Act*; consumer proposals are not possible under the CCAA. At one time, the BIA contained reorganization provisions only for companies that were bankrupt; for those that were insolvent but not bankrupt, reorganization under the CCAA was possible. At present, reorganization for insolvent corporations can occur under either statute, although the $5 million debt threshold must be met with respect to the CCAA.

The CCAA provides a relatively flexible framework that allows for reorganizations – rather than the relatively more specific rules under the BIA – and allows the Court a fairly high degree of discretion in determining how best to resolve the cases before it. The statute itself is short and relatively few guidelines are provided.

With the proclamation of Bill C-5, the CCAA was amended to align procedures under it more closely with those under the BIA.

The CCAA provides a relatively flexible framework that allows for reorganizations – rather than the relatively more specific rules under the BIA – and allows the Court a fairly high degree of discretion in determining how best to resolve the cases before it.

CHAPTER FOUR:
THE SENATE COMMITTEE'S EVIDENCE AND RECOMMENDATIONS ON CONSUMER INSOLVENCY ISSUES

A. Federal Exempt Property

When an individual becomes bankrupt and a trustee takes possession of the debtor's property in order to satisfy creditors, certain classes of property – exempt property – continue to belong to the debtor. There is a public policy rationale underlying these exemptions: these types of goods are required as basic necessities of life for the debtor and his or her family, and assist in the debtor's reintegration into society.

There is a public policy rationale underlying [exempt property]: these types of goods are required as basic necessities of life for the debtor and his or her family, and assist in the debtor's reintegration into society.

The *Bankruptcy and Insolvency Act* (BIA) establishes three categories of exempt property:

- property held by the bankrupt in trust for others;
- Goods and Services Tax credit payments and prescribed payments related to the personal needs of individuals; and
- property of the bankrupt that is exempt from seizure under provincial/territorial law where the property is situated and the bankrupt resides.

This third category – provincial/territorial exemptions – varies across jurisdictions. Nevertheless, there are certain similarities. For example, the following assets are generally considered to be exempt property, often up to some monetary limit: food; furniture; appliances; medical devices; tools required to earn an income; and a vehicle. Some jurisdictions provide an exemption for equity in real estate, while others do

… the types and values of exempt assets do vary somewhat, and some have not been updated to reflect increases in the cost of living or societal changes.

not. That being said, the types and values of exempt assets do vary somewhat, and some have not been updated to reflect increases in the cost of living or societal changes. Assets in life insurance Registered Retirement Savings Plans are also exempt from seizure under provincial/territorial law.

Since 1970, when the Study Committee on Bankruptcy and Insolvency Legislation – the Tassé Committee – recognized the benefits of a list of federal exempt property and saw no constitutional barriers to its existence yet supported continuation of provincial/territorial exemptions, there has been debate about whether a list of federal exempt property should exist, either as a substitute for lists of provincial/territorial exempt property or as an alternative to them.

Supporters of lists of provincial/territorial exempt property argue that the current system allows needed consideration of regional variations in the cost of living and property use. Opponents, on the other hand, believe that lists of provincial/territorial exempt property are inconsistent with a fundamental premise of Canada's insolvency legislation: that bankrupts and their creditors should be treated identically, regardless of residence or place of business. They believe that the current system lacks uniformity and can create inequities in the treatment of debtors; in extreme cases, it may encourage debtors to survey the lists of exempt property in all provinces/territories – in essence, to "forum shop" – and to move to the jurisdiction with the most generous list of exempt property before filing for bankruptcy. Consistent with this view, federally determined exempt property with specified monetary amounts should apply, in the same way that the Superintendent of Bankruptcy's directive with respect to surplus income is applied consistently across the country.

Witnesses provided the Committee with a range of views on the issue of federal exempt property: for, against, and as an option. The Personal Insolvency Task Force recommended a list of federal exempt property, as an alternative to provincial/territorial exempt property, that could be selected by debtors when filing for bankruptcy:

- apparel and household furnishings, to a maximum value of $7,500;
- medically prescribed aids and appliances, and medication for use or consumption by the debtor or his or her family;
- one motor vehicle, to a maximum value of $3,000 in equity;
- tools of the trade and professional books, exclusive of motor vehicles used in trade or business, to a maximum value of $10,000 in equity;
- equity in a debtor's residence, to a maximum of $5,000, with each debtor entitled to the full exemption in cases of joint filing; and
- real and personal property used by a debtor whose livelihood is derived from farming, fishing, forestry and other activities related to the natural resource sector to a value of not less than $10,000 and not more than $20,000 in equity, as governed by provincial/territorial law.

Furthermore, the Task Force recommended that the value of the exempted assets be periodically adjusted to reflect increases in the cost of living. This could occur by regulation under the BIA or, preferably, by exercise of the Superintendent's directive powers. "Trading" among different categories of exemptions – what is known as a "wild card" exemption and is an American practice – was not recommended.

Professors Ziegel and Telfer, representing a number of professors of law, voiced support for the notion of an optional list of federal exempt property, as did the Canadian Bar Association, although the latter told the Committee that it is concerned about the complexities that could be introduced with two exemption schemes. The Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada generally supported the Task

Force's proposal since, in their view, "[t]his federally prescribed list of exemptions [would] bridge the disparity that currently exists among provincial exemption levels on specific assets." They also told us that "the bankrupt must choose either one system or the other and not be allowed to 'cherry pick' between the federally and provincially prescribed exemptions."

Some of the Committee's other witnesses, however, argued that a federal list would not adequately recognize regional variations and would not ensure uniformity across Canada, but would add complexity. Omega One Ltd. told the Committee that a parallel system of federal exempt property would "add complexity for little apparent benefit. Debtors … in provinces with lower exemptions [would] likely adopt the proposed federal exemptions as a routine choice. The federal scale [would] become the *de facto* scale for those provinces. Residents of provinces with generous exemptions [would] ignore the proposed federal *schema*. There [would] remain unequal protection across Canada." In fact, in its view, irregularities regarding property rights would be created within some provinces/territories.

Advocis, formed through the merger of the Canadian Association of Insurance and Financial Advisors and the Canadian Association of Financial Planners, also does not support a list of federal exempt property. The organization told the Committee that the BIA should continue to incorporate provincial/territorial exempt property by reference; the BIA should not override those exemptions.

… we believe that a federal list of exempt property should be available as an option for bankrupts.

The Canadian Bankers Association advocated one system of property exempt from seizure, whether the provincial/territorial lists that already exist or the development of a federal list. In its view, the BIA should either maintain the status quo or include a federal list of exempt property, but not both; the bankrupt should not be able to choose between a federal list and a provincial/territorial list. The Association believes that allowing choice "would not eliminate any regional discrepancies and it would add more complexities to the process for little apparent benefit."

While the Committee respects the arguments made by witnesses who supported only a list of provincial/territorial exempt property and those who believed that the law should clearly provide for either provincial/territorial exempt property or federal exempt property but not both, we believe that a federal list of exempt property should be available as an option for bankrupts. In our view, the bankrupt should select either the federal list or the provincial/territorial list of exempt property in their locality in its entirety and at the point of filing for bankruptcy. Moreover, recognizing the argument made by some witnesses about the extent to which the value of the assets in the provincial/territorial lists have not been updated over time, we believe that adjustments should be made annually in order to recognize the effects of inflation. We feel that providing bankrupts with this option would help to ensure the fairness that we are seeking in our insolvency system, and for this reason the Committee recommends that:

We feel that providing bankrupts with [the option of a list of federal exempt property] would help to ensure the fairness that we are seeking in our insolvency system …

The Bankruptcy and Insolvency Regulations be amended to provide a list of federal exempt property. The debtor should be required to choose, at the time of filing for bankruptcy and in its entirety, either the list of federal exempt property or the list of provincial/territorial exempt property available in his or her locality. The value of the property in the list of federal exempt property should be increased annually in accordance with increases in the cost of living as measured by the Consumer Price Index.

B. Exemptions for RRSPs and RESPs

… since federal and provincial/territorial pension and insurance laws make registered pension plans and insurance policy proceeds exempt from execution and seizure, benefits from registered pension plans and Registered Retirement Savings Plans (RRSPs) associated with life insurance policies are generally exempt from seizure in bankruptcy.

Under the BIA, the property of a debtor which is exempt from seizure in bankruptcy under the laws of the province/territory in which the property is situated and the bankrupt resides is not part of the bankrupt's estate and is not available for distribution to creditors. Consequently, since federal and provincial/territorial pension and insurance laws make registered pension plans and insurance policy proceeds exempt from execution and seizure, benefits from registered pension plans and Registered Retirement Savings Plans (RRSPs) associated with life insurance policies are generally exempt from seizure in bankruptcy. That being said, there are a limited number of cases in which a debtor with exempt RRSP savings has been obliged, as a condition of discharge, to collapse a portion of his or her RRSP and to contribute the after-tax proceeds to the trustee for distribution to creditors. In Quebec, RRSPs convertible to annuities held by trust companies are also exempt.

Other types of RRSPs – such as those held by banks, brokerages or in self-directed funds, or what might be termed "non-insurance" – are generally non-exempt, unless for example they are locked in by virtue of the RRSP funds having been transferred from a pension fund on termination of employment. If the holder of a non-insurance RRSP that is not locked in becomes bankrupt, the funds become the property of the trustee and are available for distribution to creditors.

Arguments both for and against extending an exemption from seizure in bankruptcy to all RRSPs exist. Supporters point to the public policy objective of helping Canada's citizens to save for their retirement. From this perspective, if the federal government feels that this undertaking is sufficiently worthwhile that it is willing to provide tax assistance for retirement savings, then it is logical to protect retirement savings from seizure in bankruptcy, and to protect all forms of retirement savings to the same extent. This protection may be particularly important for those

employees who do not have an employer-sponsored registered pension plan and for self-employed individuals.

Opponents, however, note that exempting non-insurance RRSPs from seizure in bankruptcy would reduce the moneys available for distribution to creditors. They also observe that non-locked-in RRSPs can be used for purposes other than retirement, and that RRSP holders have the option to purchase an insurance RRSP and thereby protect those assets from seizure. Finally, opponents believe that RRSPs are a form of investment and should not be treated differently than other investments; if RRSPs are exempt from seizure in bankruptcy, then other investments should be similarly exempted.

Opponents, however, note that exempting non-insurance RRSPs from seizure in bankruptcy would reduce the moneys available for distribution to creditors.

Witnesses provided the Committee with recommendations both for and against exempting non-insurance RRSPs from seizure in bankruptcy. The Personal Insolvency Task Force pointed out that the federal government has made a policy choice in deciding to provide individuals with an incentive to save for their retirement. In particular, incentives exist through the exempt status given to registered pension plans and the tax treatment of registered pension plans and Registered Retirement Savings Plans, among others. It argued that "it would be inappropriate if the bankruptcy system treated RRSPs in exactly the same way as pensions … because there are several key differences that call for different treatment." For example, pension contributions are usually compulsory, periodic and fixed in amount, while RRSP contributions are voluntary, often irregular and self-determined in amount. As well, registered pension plans generally cannot be accessed until retirement, while RRSPs can be collapsed at any time, unless they are locked in, and may be used for reasons unrelated to retirement.

While the Task Force believed that "the BIA ought not to be available for strategic use by those who intend to shelter their assets from the reach of impending or foreseeable creditors," it also shared the view that "[i]t would be consistent with both retirement and bankruptcy policies if bankruptcy legislation afforded exempt status to RRSP

savings that have accumulated through prudent retirement savings practices before the period of insolvency." Consequently, the Task Force recommended that legislative change occur in order that RRSPs would be eligible for exemption in bankruptcy, subject to a number of requirements, including: locking in to ensure that funds are used, subject to exceptions in cases of financial hardship, for retirement; non-exempt status for contributions made in the three years prior to bankruptcy in order to prevent strategic behaviour and to allow seizure of those moneys that reasonably could have been used for debt repayment; treatment of the proceeds from a locked-in RRSP as income subject to surplus income standards; and a cap on the exemption, tied to the debtor's age and the maximum RRSP contribution limit in the year of bankruptcy, so that older bankrupts would be able to protect more of their retirement savings.

The Canadian Bar Association expressed general support for the Task Force's proposal, but advocated a two-year clawback and no cap; if a cap were to be imposed, however, the Association felt that it should be adjusted periodically. It supported locking in until retirement because "[a] policy that helps to discourage withdrawals prior to retirement would be socially beneficial … [T]here is no policy justification for exempting savings accounts not earmarked for retirement." Similarly, the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada were generally supportive of the Task Force's position, but argued for a clawback of the lesser of the contributions in the three-year period and the realizable value in the RRSP at the end of bankruptcy.

An exemption for RRSPs was also supported by the Canadian Federation of Independent Business, which told the Committee that the majority of its members are "clearly in favour." Advocis also indicated that equitable treatment of retirement savings should occur, and suggested that "[i]ndividuals who save for their retirement in whole or in part through RRSPs or [Deferred Profit Sharing Plans] or who receive retirement income from [Registered Retirement Income Funds] or annuities funded by proceeds from those

registered plans should enjoy similar protection from creditors as individuals who fund their retirement through [registered pension plans]." Protection would be made available to a larger number of individuals, which may be of particular benefit to employees of small employers, who may lack a registered pension plan, or self-employed individuals with a modest income.

The organization also believes that income acquired from an RRSP, Deferred Profit Sharing Plan (DPSP) or Registered Retirement Income Fund (RRIF) should be protected to the same extent as pension income from a registered pension plan. It also commented on the Task Force's recommendation regarding non-exempt status for contributions made in the three years prior to bankruptcy. In particular, it rejected "the presumption of the [Task Force] that all new contributions to a protected RRSP made within three years preceding bankruptcy will be fraudulent conveyances intended to defraud a creditor."

In the view of the Alberta Law Reform Institute, "[t]here is an unfairness in [the] exposure of non-insurance RRSPs, compared to the virtually complete protection of insurance RRSPs and annuities, and most pensions." In essence, the Institute believes that "insurance and non-insurance RRSPs, DPSPs and RRIFs …, and obligations to pay money out of such plans, should be totally exempt from all judgment creditors' remedies. No distinction should be drawn among remedies nor should the exemption be different between insurance and non-insurance products." Finally, noting that many – and perhaps most – debtors have no RRSP or have already collapsed it, the Institute argued that the "practical impact of a total exemption is likely to be minimal in most situations."

The Canadian Bankers Association shared with the Committee its view that a level playing field should be created among retirement savings and income products and indicated that the law should "[make] such products either subject to seizure in bankruptcy or exempt from seizure in bankruptcy."

[The Committee was told that with an exemption for RRSPs, protection] would be made available to a larger number of individuals, which may be of particular benefit to employees of small employers, who may lack a registered pension plan, or self-employed individuals with a modest income.

The Association advocated additional research to determine if an exemption of non-insurance RRSPs from seizure in bankruptcy is an issue that needs to be addressed through legislative amendment.

The Committee found arguments made by those witnesses who urged uniformity of treatment of retirement savings quite compelling.

The Committee found arguments made by those witnesses who urged uniformity of treatment of retirement savings quite compelling. In our view, the public interest is served when Canadians save for their retirement. While some Canadians are able to do so through a registered pension plan available as deferred compensation from their employer – perhaps augmented by private savings and Registered Retirement Savings Plans – those who do not have access to a registered pension plan and those who are self-employed must rely on RRSPs.

As noted above, proceeds from a registered pension plan and some RRSPs – notably those associated with insurance policies and those that are locked in – are generally protected from seizure. The Committee is concerned about the inequity: the inequity between the treatment of registered pension plans and RRSPs, and the inequity between insurance RRSPs and non-insurance RRSPs. In our view, with this differential treatment in the latter case, there is some danger that protection would be given only to those RRSP holders who perhaps were debtors anticipating a future bankruptcy or who had received more expert financial advice. That being said, we are also fully aware of the differences that exist between registered pension plans – which are deferred compensation – and most RRSPs – which are a retirement savings vehicle that generally cannot be viewed as deferred compensation. Moreover, we are also aware that registered pension plans provide primarily retirement benefits and that contributions are locked in until that time, while funds in RRSPs that are not locked in can currently be used for purposes that are not restricted to retirement, since they can also be used for home purchases and education under certain circumstances or collapsed and used for other purposes.

In the past, in particular during our examination of Bill C-5, the Committee expressed support for exempting all

RRSPs from seizure in bankruptcy, subject – of course – to appropriate measures to prevent abuse. In seeking uniform treatment that would make exemption rules more equitable and provide consistent protection to all RRSPs, regardless of their type, we urged the federal government to address the inequities that exist between insurance and other RRSPs.

Fairness to debtors requires equitable treatment among retirement savings vehicles, while fairness to creditors requires that RRSPs be locked in and that contributions in the year prior to bankruptcy – when the funds could reasonably have been used to pay debts – be available to satisfy their claims.

The Committee's views have not changed. We continue to believe that amendments are needed to ensure fairness. Fairness to debtors requires equitable treatment among retirement savings vehicles, while fairness to creditors requires that RRSPs be locked in and that contributions in the year prior to bankruptcy – when the funds could reasonably have been used to pay debts – be available to satisfy their claims. From this perspective, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to exempt funds in all Registered Retirement Savings Plans from seizure in bankruptcy, provided that three conditions are met: the Registered Retirement Savings Plan is locked in; contributions made to the Registered Retirement Savings Plan in the one-year period prior to bankruptcy are paid to the trustee for distribution to creditors; and the exempt amount is no greater than a maximum amount to be set by regulation and increased annually in accordance with increases in the cost of living as measured by the Consumer Price Index.

Education Savings Plans, previously known as Scholarship Trust Plans, have existed in Canada for more than four decades as a vehicle to save funds to finance the cost of future post-secondary education of children. Capital was returned to the plan holder, while the income on the capital was paid in the form of a scholarship to students pursuing post-secondary studies at a degree-granting institution. Income earned in the Plan was attributed to the plan holder as earned income, and was taxed. During the 1970s, tax sheltering for funds held in these Plans resulted in the development of Registered Education Savings Plans (RESPs).

Except in special circumstances, proceeds from an RESP may only be used to finance post-secondary education.

In 1998, the federal government created the Canada Education Savings Grant (CESG), which has increased participation in RESPs. Under the program, the government matches up to 20% of the first $2,000 contributed annually by Canadian residents to an RESP. The Grant may only be paid to students attending approved post-secondary institutions. By the end of 2000, there were approximately 1.7 million RESP contracts with more than $7.1 billion in assets under administration, up from about 700,000 contracts with about $2.4 billion in assets three years earlier.

In the event that the RESP plan holder becomes bankrupt, the trustee withdraws the contributions made by the plan holder and the Canada Education Savings Grant is returned to the federal government.

Believing that RESPs serve the public interest by encouraging a more highly educated population, some have argued that RESP funds should be exempt from seizure in bankruptcy; in their view, federal assistance to RESPs and support through the CESG indicate the importance that is placed on education. Others, however, suggest that granting such an exemption would disadvantage creditors by reducing the moneys available for distribution to them and eroding the principle of a fair distribution of assets in bankruptcy. As well, in their view, RESPs could be viewed as an investment, which should receive the same treatment in bankruptcy as other investments.

Believing that RESPs serve the public interest by encouraging a more highly educated population, some have argued that RESP funds should be exempt from seizure in bankruptcy …

The Committee received testimony from the RESP Dealers Association about the treatment of Registered Education Savings Plans when the plan holder becomes bankrupt. The Association suggested that, with the rapidly increasing costs of post-secondary education, "RESPs are often the only secure investment vehicles that children have to fund their post-secondary education needs. Against this background, all funds (principal, interest, CESG) should be

fully protected and shielded from creditor seizure in the event of a bankruptcy filing." In its view, "the concept of shielding RESPs from creditor seizure is akin to shielding life insurance policies which already receive protection." According to the Association's calculations, the maximum that would be shielded from creditors over a span of an average Plan duration of 15 years would be $19,649 in principal, interest and Canada Education Savings Grant contributions.

The Association also noted the need to strike an "equitable balance … between the promotion of consumer protection rights and securing the rights of creditors." From this perspective, it recommended that any new RESP opened, or any non-standard principal contributions made, within one year or less of the date of bankruptcy filing should not be accorded any level of protection. Finally, because of the existence of different client categories, it recommended different levels of protection for the custodial parents of a beneficiary and persons other than the custodial parents of the beneficiary.

The Committee, too, supports the notion of a highly educated workforce and believes that there is a federal role in this regard. In our view, however, it is not appropriate for the funds in an RESP to be entirely protected from seizure in the event of the plan holder's bankruptcy. In addition to the CESG, the federal government has a variety of grants and loans that assist students in pursuing post-secondary education. In this instance, our focus is on fair treatment for both creditors and the beneficiaries of RESPs. Fairness for creditors suggests that the moneys available for distribution to them should be as great as is reasonably possible, while fairness for the beneficiaries of RESPs suggests that they should be able to access moneys that have been saved for their education. We believe, as we did with RRSPs, that the funds should be locked in as a means of ensuring that they are used for the intended purpose – education – and that contributions in the year prior to bankruptcy should be available to satisfy creditors claims, since those contributions

In our view, however, it is not appropriate for the funds in an RESP to be entirely protected from seizure in the event of the plan holder's bankruptcy.

could reasonably have been available to pay debts. Consequently, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to exempt funds in a Registered Education Savings Plan from seizure in bankruptcy, provided that two conditions are met: the Registered Education Savings Plan is locked in; and contributions made to the Registered Education Savings Plan in the one-year period prior to bankruptcy are paid to the trustee for distribution to creditors.

C. Reaffirmation Agreements

A reaffirmation agreement is an agreement between a bankrupt and his or her creditor(s) to reaffirm – or revive – responsibility for pre-bankruptcy debts that have been discharged. Reaffirmation can occur through conduct or through express agreement. The first type of reaffirmation occurs when the bankrupt continues to make payments to creditors following the discharge of the relevant debts; the Court has interpreted this conduct by the bankrupt as re-establishing his or her promise to make payments. The second type of reaffirmation occurs when bankrupts expressly enter into written agreements with creditors to repay discharged debts. The Court is likely to enforce these agreements where sufficient or new consideration is offered, such as the granting of new credit.

A number of considerations exist with respect to such agreements. One issue is the extent to which reaffirmation agreements of either type are occurring within Canada. No data are available, although anecdotal evidence suggests that reaffirmation is occurring as a condition of new credit. As well, there may be reasons why a discharged bankrupt might want to make payments voluntarily; consider, for example, loans that have been made by relatives or creditors with whom the debtor has had a longstanding relationship. There is some concern that reaffirmation of discharged debt undermines the fresh start principle, although it may be the sole means by which a bankrupt can obtain credit and in some cases may be in the best interest of both parties.

No data are available, although anecdotal evidence suggests that reaffirmation is occurring as a condition of new credit.

At present, the BIA is silent on the issue of reaffirmation agreements, although the Court has permitted such agreements in certain circumstances.

The Committee received arguments from witnesses both for and against reaffirmation agreements. Regarding reaffirmation by conduct, the Personal Insolvency Task Force told the Committee that "bankrupts did not, in general, intend to reaffirm their pre-bankruptcy promises; instead, they

probably continued to make the payments in order to retain possession of the leased or mortgaged asset and did not appreciate that they were reaffirming their covenant to pay." It recommended that reaffirmation agreements in respect of unsecured transactions be prohibited in all circumstances and prohibited except subject to certain conditions in respect of secured transactions; the conditions are related to such matters as the possession of the asset when the written reaffirmation agreement is signed, limits on the amount that can be reaffirmed, time limits within which reaffirmation can occur, and an opportunity for a bankrupt to rescind a reaffirmation within a certain period of time.

[The Committee learned that] there is also the danger that discussions between debtors and creditors may occur at a point of relative vulnerability of debtors, who might be susceptible to pressure.

The Task Force also believed that it should be an offence, under the BIA, for a creditor who knows about a bankrupt's discharge to accept payment of any indebtedness released upon the bankrupt's discharge, except in certain circumstances, including voluntary payments made by a discharged bankrupt to a relative. Moreover, it recommended that reaffirmation not occur through the continuation of payments or through any other conduct, since decisions by bankrupts in this regard may be uninformed. In general, the Task Force's view was that reaffirmations are inconsistent with the fresh start principle. There is also the danger that discussions between debtors and creditors may occur at a point of relative vulnerability of debtors, who might be susceptible to pressure.

Supporting the general thrust of the Task Force – if not its recommendations, which they view as too complex and probably unworkable in practice – Professors Ziegel and Telfer shared their view that "abuses in reaffirmation agreements need to be curbed." They identified the need for further study of existing reaffirmation practices in Canada.

The Canadian Bar Association supported only the Task Force's proposal with respect to reaffirmation by conduct, arguing that "[r]eaffirmation should not occur through unconscious or unknowing acts," and expressed concern about limiting the individual autonomy of Canadians without exploring other, less intrusive, means of controlling the alleged

abuse. In its view, "there is insufficient evidence or justification at this time to warrant regulating voluntary reaffirmations at all."

The Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada, on the other hand, did not support the Task Force's position, and advocated greater study into the scope and frequency of reaffirmation agreements and the correct policy response.

Omega One Ltd. told the Committee that, in its opinion, there are "very few attempts by arm's-length creditors to obtain payment for an unsecured debt that was previously discharged by bankruptcy. … In our experience, this practice (while very rare) is usually generated by a customer request. … Canadian credit providers will usually accept gratuitous repayment for previously discharged debts, but the offer must come from the customer and there must be no coercion." Perceiving that this situation is not problematic, the organization felt that legislative provisions are unnecessary.

The Canadian Bankers Association, too, argued that "[t]here should be no legislation put in place to prohibit such agreements. It should be left to individual consumer choice whether they wish to repay a debt after that debt has been extinguished. … Some borrowers want to redeem their standing with a particular creditor and this should be allowed." It suggested that credit counselling can be used to "prevent unscrupulous creditors from taking advantage of bankrupts."

The fresh start principle is a hallmark of insolvency law in Canada. From this perspective, individuals who declare bankruptcy are able to begin again, with only their non-dischargeable debts. Reaffirmation agreements are inconsistent with this principle. In the Committee's opinion, banning reaffirmation agreements is simple, consistent with the fresh start principle and supports the objective of fairness in the distribution of assets, which would be undermined if

In the Committee's opinion, banning reaffirmation agreements is simple, consistent with the fresh start principle and supports the objective of fairness in the distribution of assets …

some creditors continued to receive payment under such an agreement but others did not. This approach would also contribute to the goal of predictability, since reaffirmation agreements would be disallowed in all cases. For these reasons, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to prohibit reaffirmation by conduct or by express agreement.

D. Summary Administration

Canada has had a simpler and less expensive bankruptcy process for consumer debtors with few assets since 1949. Before the 1992 amendments to the BIA, only debtors with assets valued at less than $500 could use the summary administration – or simplified – process. Recognizing, however, that many debtors had minimal exempt unsecured assets and that a simpler, less expensive bankruptcy process was needed for them, amendments to the BIA in 1992 raised the asset threshold to $5,000, thereby enabling more debtors to use the simplified process. Since then, the asset threshold has been increased again, to $10,000, and the summary administration procedure was used in more than 96% of the bankruptcies administered by the Office of the Superintendent of Bankruptcy (OSB) in 2002, an increase from 83.2% in 1987.

… the summary administration procedure was used in more than 96% of the bankruptcies administered by the Office of the Superintendent of Bankruptcy (OSB) in 2002, an increase from 83.2% in 1987.

In the summary administration process, some of the requirements of the ordinary process are either streamlined or eliminated; for example, newspaper bankruptcy notices are not required, creditor meetings are held only on request and there is no requirement that inspectors be appointed. The trustee does, however, hold an initial assessment interview with the debtor, send documents to creditors and prepare a report that includes information on the bankrupt's affairs, the causes of the bankruptcy, the debtor's conduct before and after the bankruptcy, and a recommendation regarding whether the debtor should be automatically discharged after nine months in bankruptcy. The OSB and creditors may oppose the trustee's recommendation and/or the debtor's discharge.

The ordinary administration procedure is used where the bankrupt's realizable assets will exceed $10,000. With this process, creditors meet and may confirm the appointment of the trustee selected by the debtor or may appoint a trustee selected by them. They may provide the trustee with directions about the administration of the bankrupt's estate, and may vote on the appointment of inspectors to assist the trustee.

As noted earlier, the Personal Insolvency Task Force made a number of recommendations for change regarding procedural issues in consumer proposals and bankruptcies, many of which would provide a more streamlined and less costly process if adopted, since they would allow the parties involved to choose their level of involvement on the basis of "by exception rather than by rule." The recommendations are not discussed here, but are presented in Chapters 4 and 5 of its report.

In presenting its view on the summary administration process, the Canadian Bankers Association suggested that the Task Force's proposal "provides a reasonable balance between keeping costs down and protecting the integrity of the process." It, too, identified the cost savings that would likely result with streamlining, and noted that these savings should increase disbursements to creditors. Describing the proposed changes as "reasonable and appropriate," the Canadian Bar Association also advocates the adoption of the recommendations in Chapters 4 and 5 of the Task Force's report. Finally, the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada argued for an increase in the asset value permitted under summary administration to $15,000. They believed that the amount should be "updated so as not to exclude people unnecessarily."

We believe … that there is a need not only to take action to minimize the number of bankruptcies, but also to ensure that cases that do arise are addressed as effectively and efficiently as possible, while ensuring the ongoing integrity of the insolvency system.

The Committee is aware that bankruptcy cases are rising in Canada, that the Office of the Superintendent of Bankruptcy is facing resource constraints, and that more cases generally means higher costs – both economic and societal – for all. We believe, therefore, that there is a need not only to take action to minimize the number of bankruptcies, but also to ensure that cases that do arise are addressed as effectively and efficiently as possible, while ensuring the ongoing integrity of the insolvency system. In view of our desire to respect the fundamental principles of efficiency and effectiveness, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be reviewed in order to eliminate all unnecessary procedural requirements and to provide parties to a bankruptcy with an opportunity – to the extent possible – to choose their level of involvement in accordance with a "by exception rather than by rule" approach. Moreover, the use of electronic communication should be encouraged in order to simplify and expedite the insolvency process.

E. Non-Purchase Money Security Interests in Exempt Personal Property

In most provinces/territories, creditors can take security on personal property located in a person's home, even though that property would otherwise be exempt under provincial/territorial law from seizure in bankruptcy or in the event of a consumer proposal. For example, consumer loan companies may – as a condition of granting a loan – take a security interest in household goods or vehicles, even if the credit is unrelated to the purchase of those items and the items are exempt from seizure in bankruptcy. This security interest is also known as a lien or a non-purchase money security interest in exempt personal property. It differs from a purchase money security interest, where the goods bought with the credit are the security.

There has been some criticism of this practice, since it is possible that such lenders could threaten to repossess the household property – even if limited in value – in order to perhaps obtain better treatment than other creditors and perhaps more than the property is worth at fair market value. In essence, intimidation may be used by the lien holder to obtain a preference. Trustees may also feel pressured to satisfy lien holders ahead of other creditors in order to ensure that the debtor and his or her family retain their personal property. In general, problems such as these arise in relation to motor vehicles.

The BIA does not contain provisions to protect a bankrupt's personal property that would otherwise be exempt under provincial/territorial law.

The BIA does not contain provisions to protect a bankrupt's personal property that would otherwise be exempt under provincial/territorial law. Provincial/territorial consumer legislation has application to these issues, but some feel that additional controls are also needed.

Witnesses shared a variety of views on this issue. The Personal Insolvency Task Force studied non-purchase money security interests in exempt personal property and

recommended that the BIA be amended to avoid such interests in property that would otherwise be exempt from seizure. In its view, the proposal should apply to consumer proposals as well as bankruptcies, and should "extend to all non-purchase money security interests in exempted property intended for use or consumption of the debtor or the debtor's family, including apparel, household furnishings and motor vehicles." Regarding motor vehicles, it believed that the provisions should apply to any motor vehicle owned by a debtor that is exempted from the assets to be divided among creditors. In the event that the value of creditors' non-purchase money security interests in apparel and household furnishings exceed the value of the exemption provided in the BIA, the debtor should select the items that are to be exempt from seizure; regarding a motor vehicle, the lender should be required to pay the debtor the exempted amount before he or she can enforce the security interest.

Moreover, the Task Force informed the Committee that "the non-uniformity in the provincial treatment of this important aspect of exemption legislation will continue in the foreseeable future [and] justifies the need for a federal provision to ensure that all bankrupts, and those making consumer proposals, will have a uniform level of protection."

Professors Ziegel and Telfer supported the avoidance of non-purchase money security interests in exempt household goods and vehicles, as did the Canadian Bar Association, the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada.

Expressing a different view, the Canadian Bankers Association opposed any change that would render unenforceable such security interests. In its opinion, if lenders have security over non-household goods, they should be able to realize on the security in accordance with the agreement reached with the debtor; otherwise, credit availability could be reduced and the cost of credit could rise. The Association did, however, support measures that would prevent the use of coercive tactics.

… the Committee believes that the proposal made by the Personal Insolvency Task Force has merit.

Like a number of our witnesses, the Committee believes that the proposal made by the Personal Insolvency Task Force has merit. It would ensure a uniformity of protection across Canada, would safeguard the basic necessities of life for an insolvent debtor and his or her family, and could reduce problems arising from reaffirmation agreements. In essence, the fundamental principles of fairness, predictability and consistency would be assisted. As a consequence, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to prohibit non-purchase money security interests in property that would otherwise be exempt from seizure in bankruptcy. Property should be defined to include exempted property intended for use or consumption by the debtor or the debtor's family, and should encompass apparel, household furnishings and motor vehicles owned by the debtor.

F. Mandatory Counselling

At present, first-time bankrupts must undertake two mandatory counselling sessions prior to receiving an automatic discharge from their dischargeable debts; counselling is also required with respect to consumer proposals. Costs are paid out of the bankrupt's estate, which in essence means that creditors are financing the counselling sessions, since the moneys available for distribution are thereby reduced. It is thought that counselling has been effective in: helping insolvent debtors to manage better their financial affairs; changing behaviour; and developing skills and acquiring knowledge. Given the timing of mandatory counselling, however, it is perhaps most useful in helping to avoid future problems; earlier sessions might be considered as a mechanism to help debtors avoid insolvency and thereby reduce the possibility of bankruptcy. As well, it should be noted that a debtor may become insolvent even if he or she has exemplary financial management skills, since insolvency is often related to an unforeseen personal or business event.

It is thought that counselling has been effective in: helping insolvent debtors to manage better their financial affairs; changing behaviour; and developing skills and acquiring knowledge.

In general, the Committee's witnesses supported the concept of counselling. Credit Counselling Canada told us that "individuals who make a consumer proposal or file for bankruptcy [should] be compelled to attend compulsory counselling sessions given by properly trained credit counsellors." In its view, individuals "benefit tremendously" from this counselling, which is "an important component in the financial rehabilitation of individuals."

The organization also shared with the Committee the importance of properly trained counsellors and suggested the establishment of standards in order to ensure some uniformity in the level of counselling; in its view, training must go beyond the BIA Insolvency Counsellor's Qualification Course. Credit Counselling Canada also believed that the timing of the counselling sessions should be re-evaluated, and recommended the addition of a third mandatory session.

A third mandatory counselling session was also suggested by the Union des consommateurs, which

commented more generally on the lack of standardization of the content and duration of these sessions. The group also recommended fines for trustees who fail to give mandatory counselling, with the moneys used "to develop training programs and to support outreach campaigns, or to fund consumers' associations offering services across Canada."

Professors Ziegel and Telfer argued that if mandatory counselling provisions are retained, they should be "matched by provisions addressing irresponsible credit granting practices and (i) authorizing courts, *inter alia*, to subordinate creditors' claims against the estate where the creditor has shown clear carelessness or recklessness in extending credit to the consumer debtor, and (ii) extending the powers of inquiry of the Superintendent of Bankruptcy to include credit granting practices." In their opinion, there is a "striking disparity between requiring consumer insolvents to receive credit counselling while no restrictions are imposed on the credit granting practices of retailers, lenders, and credit card companies." They also support federally sponsored studies of the effect of credit counselling on bankruptcy, and credit education for consumers, including earlier in their careers and at the high school level.

Finally, the Canadian Bankers Association supported counselling provided by an independent party in order to ensure that borrowers are educated about their alternatives, and the pros and cons of each. It recommended that consideration be given to amending the BIA to require mandatory independent counselling prior to declaring bankruptcy.

The Committee strongly believes that prevention is better than a cure. While we recognize that insolvency often occurs for reasons completely unrelated to financial management skills, we hold the view that mandatory counselling is important in helping bankrupts to avoid future financial difficulties.

The Committee strongly believes that prevention is better than a cure. While we recognize that insolvency often occurs for reasons completely unrelated to financial management skills, we hold the view that mandatory counselling is important in helping bankrupts to avoid future financial difficulties. The timing and content of counselling is, however, the key to success, and we wonder whether the mandatory counselling required for automatic discharge may be, in some sense, "too little too late." That being said, we support mandatory counselling as a contributor to the

principles of responsibility and fairness. We, as a nation, have a responsibility to help our citizens avoid financial difficulty, if we can, and citizens have a responsibility to do what they can to avoid the insolvency that has social and economic costs for themselves, their families and our country. In fairness, we must help each other avoid these costs. It is for these reasons that the Committee recommends that:

In fairness, we must help each other avoid [the social and economic] costs [associated with bankruptcy].

The *Bankruptcy and Insolvency Act* be amended to require the completion of mandatory counselling by first-time and second-time bankrupts as a condition of automatic discharge from bankruptcy available after 9 and 21 months respectively. Debtors making a consumer proposal should also undertake mandatory counselling. The nature and timing of mandatory counselling should be examined to ensure its effectiveness.

G. Consumer Liens

Consumers often must leave a deposit with a retailer in partial payment for goods or services to be delivered or provided at a later date; in some cases, the consumer will pay for the good or service in full, but will await delivery. If the vendor goes bankrupt before the goods or services are received by the consumer, he or she generally has an unsecured claim and no realistic chance of recovery.

Consumer liens exist in order to protect to consumer depositors who may not view themselves as creditors and who do not intend to incur risk.

Consumer liens exist in order to protect consumer depositors who may not view themselves as creditors and who do not intend to incur risk. These liens rank ahead of secured claims and protect a particular group of creditors at the expense of other creditors. As well, they may affect the availability and cost of credit. Like non-purchase money security interests, the issue of consumer creditors can be addressed in provincial/territorial legislation.

At present, the BIA contains no provision for consumer liens.

The Consumers Association of Canada made the point that "[i]n commercial transactions (business to business) the assumption is usually made that the parties to a transaction, whether it be a loan or extending credit for the purchase of goods and/or services, are in a position to assess the risk, or to seek appropriate assistance, and make an informed decision. In a consumer to business transaction … the positions of the participants are not equivalent. Even when following the basic principle of 'caveat emptor'/buyer beware and avoiding situations which appear to be risky, the consumer is basically at the mercy of the vendor."

The Association cited examples of consumers who purchase advance tickets to public performances that are subsequently cancelled and air travellers who purchase a ticket to fly on an air carrier that subsequently ceases operations.

Similar situations arise when consumers make deposits on merchandise that is unavailable at the time but will be delivered in the future, and when they purchase goods for future delivery or use. In its view, consumer protection legislation is deficient, and any moneys given to a vendor for future goods or services should be returned; in effect, the moneys have been held in trust and should not be included among the assets seized and subsequently liquidated by the trustee.

The Canadian Bankers Association, however, suggested to the Committee that the BIA should not be amended to enact a consumer lien provision. In its view, such a change would limit credit availability and increase borrowing costs. Moreover, efficiency would be affected, since creditors would be unable to determine accurately the financial position of borrowers.

While the Committee has sympathy for individuals who find themselves disadvantaged when a vendor to whom they have given a deposit or made a purchase for future delivery becomes bankrupt, we believe that it would be inappropriate for the issue to be addressed within federal legislation. As well, it is our view that protecting a particular group of creditors at the expense of other creditors is perhaps unfair, could affect efficiency, and should only occur after very careful consideration of any unintended consequences that might result. For these reasons, the Committee recommends that:

… it is our view that protecting a particular group of creditors at the expense of other creditors is perhaps unfair, could affect efficiency, and should only occur after very careful consideration of any unintended consequences that might result.

The issue of consumer liens continue to be addressed within provincial/territorial consumer protection legislation.

H. Student Loans

Evidence reveals that a minority of student loan borrowers in Canada experience severe difficulty in repaying their student loans, and those that default do so not because they do not want to pay their debt, but rather because their financial situation is such that they cannot pay. Moreover, those that file for bankruptcy and have student loan debt are thought to have a more difficult financial situation than that of the average person who seeks bankruptcy protection.

Canada has a long history of assisting students who wish to pursue post-secondary education.

Canada has a long history of assisting students who wish to pursue post-secondary education. For almost four decades, the federal government has assisted needy students through loans that are interest-free while they are in school, with a six-month grace period after leaving school before interest payments are required. At present, about 350,000 students annually benefit from the federal Canada Student Loans Program, and the majority of these students repay their loans in full and on time. As noted below, those that are unable to do so can access a variety of debt management measures to help avoid bankruptcy. Students may also access provincial/territorial student loan programs.

In the last decade, relatively significant changes have occurred with respect to the treatment of student loans under the BIA, perhaps because of rising levels of default among student loan holders in the early 1990s. In the 1990-1991 period, more than 5,600 borrowers holding $40.5 million in student loans declared bankruptcy. Five years later, about 11,000 borrowers filed for bankruptcy; they held more than $100 million in student loans. Over the 1990-1997 period, about 53,000 borrowers declared bankruptcy or participated in a bankruptcy-related event, holding about $445 million in federal student loans at the time; most did so within seven years after leaving school. This bankruptcy activity meant losses for governments and, through them, for taxpayers.

Prior to 1997, student loan debt was treated in the same manner as other consumer debt; in general, student loans were discharged along with other debt provided the trustee or creditor did not believe that students were abusing the system, in which case they could oppose the discharge or creditors could refuse to accept a consumer proposal.

Amendments to the BIA that took effect in September 1997, however, changed the status of student loan debt and, some believe, moved the insolvency system away from the goal of reducing the extent to which any particular class of creditors receives special treatment under the Act. In particular, student loan debts were made non-dischargeable if a debtor filed for bankruptcy before ceasing full- or part-time studies or within two years after studies were completed. A debtor who went bankrupt during the two-year period could, however, apply to the Court at the end of the period for discharge of his or her student loan debt; the Court could order a discharge if the student demonstrated that he or she had acted in good faith in trying to repay the debt but was unable to do so and repayment would result in significant hardship. Those who filed for bankruptcy after the two-year period could have their student loans discharged in a manner similar to other consumer debt during the bankruptcy process. It is thought that the change was made, in part, in order to safeguard the sustainability of the Canada Student Loan Program.

Amendments to the BIA that took effect in September 1997, however, changed the status of student loan debt and, some believe, moved the insolvency system away from the goal of reducing the extent to which any particular class of creditors receives special treatment under the Act.

Also in that year, the federal Budget extended the period for which eligible borrowers meeting certain income requirements could receive interest relief. In particular, the period was increased from 18 to 30 months and made available throughout the loan repayment period. As well, no interest or principal payments are required when receiving interest relief, and interest does not accrue.

Amendments to the BIA in 1998 increased the two-year period during which student debt could not be discharged to ten years. Other changes were also made to the Canada Student Loans Program as a consequence of the 1998 federal Budget, and these were thought to provide students

with assistance that would help them to avoid bankruptcy induced by their student loan debt. Interest relief periods were again extended, so that students with income below the established income thresholds – which were increased by 9% – could be eligible for up to 54 months of interest relief within the first five years of completing their studies which, when combined with the six-month grace period, allows the deferment of payments on interest and principal for the first five years after leaving school. Moreover, federal income tax credits on interest paid on government student loans were created, and a debt reduction in repayment measure was introduced. Two grant programs were also established, including the Millennium Scholarship Fund providing students with non-repayable grants.

More recently, the 2003 Budget announced enhancements to the debt reduction in repayment program by, among other initiatives, removing the restriction that limited debt reduction to 50% of outstanding debt, so that borrowers are now eligible for an initial loan remission of up to $10,000, and by creating an additional reduction of up to $5,000 one year after the initial debt reduction if the borrower is still in financial difficulty, with a further reduction of up to $5,000 available two years after the first reduction if the financial difficulty continues to exist. Moreover, students who default on their Canada Student Loans or who have declared bankruptcy have access to interest relief.

Views on the treatment of student loan debt in discharge are diverse.

Views on the treatment of student loan debt in discharge are diverse. Some believe that the ten-year period is too onerous, and that it is inconsistent with the fresh start principle, the public interest aspect of a highly educated workforce and the principle that all types of consumer debt should be treated similarly. Others, however, feel that incentives are needed to prevent abuse and to ensure that governments, and through them taxpayers, do not experience unacceptable loan losses.

The Personal Insolvency Task Force noted arguments both for and against the special treatment of the discharge of student loan debt. Arguments against immediate

dischargeability include: former students may be insolvent only temporarily, and do have the ability to repay their loans because they will have higher-than-average income in the future; allowing immediate discharge would increase federal and provincial/territorial government student loan losses; and debt relief – such as the interest and debt relief programs offered by the federal and some provincial/territorial governments – is available to former students that should reduce the extent to which bankruptcy is required.

Regarding these arguments, the Task Force made the point that while the interest and debt relief programs do provide relief that is not available to other debtors, they "are not a replacement for bankruptcy as a method of providing a 'fresh start'." Moreover, the Canada Customs and Revenue Agency could also face large losses that "could be relieved by prohibiting debtors from discharging their debts. Why should those making student loans receive special treatment?"

Arguments also exist, however, to support the immediate discharge of student loan debt, including: student loans are no different than other dischargeable consumer debt; the non-dischargeable nature of student debt constitutes discrimination on the basis of age, which is a violation of the *Canadian Charter of Rights and Freedoms*; and some debtors experience particular hardship that makes repayment of their student loans virtually impossible.

After consideration of these arguments, the Task Force recommended that – with respect to both consumer proposals and bankruptcy – the BIA be amended in order to: reduce the length of time prior to discharge of student loans to five years after the conclusion of full- or part-time studies; allow, on the basis of a Court-administered hardship hearing, the discharge of student loans at any time more than one year after the completion of full- or part-time studies; and clarify that partial discharge of student loans is allowed as a consequence of a Court-administered hardship hearing.

Most of the Committee's witnesses supported the general thrust of the conclusions reached by the Task

Force, and told the Committee that the current treatment of student loan debt is burdensome. From their perspective, the requirement that students must wait ten years before their student loan debt can be discharged is too onerous and should be eliminated or, at a minimum, shortened. Moreover, some believe that student debt should not be treated differently than other debt in bankruptcy, and that the Court should be able to discharge debt more expeditiously in cases of exceptional circumstances.

Credit Counselling Canada argued for a "significant reduction" in the ten-year period, and suggested that "[t]he ten-year period during which discharge … is not allowed is often a period of social atrophy. With this and often other debts a financially struggling individual faces a form of economic void as he or she wades through the waiting period. The individual is thus neither able to pay the debt, nor is he or she able to move on under the traditional auspices of bankruptcy proceedings. … [A] person in these circumstances should not face such a needless period of unproductivity." As well, it believed that student loans should not be treated in a significantly different manner from other dischargeable personal debts.

Professors Ziegel and Telfer also argued for earlier discharge of student loans, and the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada supported the Task Force's recommendations. The groups also recommended, however, an amendment to the BIA to define clearly what constitutes "studies." In their view, "[t]here should also be a clear definition of when the bankrupt has left school, perhaps linking the discharge period to the specific study program or period for which the loan was given. This issue requires further study."

The onerous nature of the ten-year period was echoed by Ms. Viola Doucet, a non-discharged bankrupt with student debt, who told the Committee that "[individuals with student debt] need a way out, and to wait 10 years is not reasonable. Our lives are on hold. That is why we are here today, to

support the change [to] 5 years [and to argue for such individuals] to present themselves [to] a judge to be discharged … earlier [in exceptional cases], because no matter how long they wait, their situation will not get any better." The frustration that some individuals with student loans feel was also presented to us by Ms. Lori Gravestock who, with a high level of student debt, said that "[f]iling for bankruptcy seems to be my only option."

The frustration that some individuals with student loans feel was also presented to us … .

Ms. Doucet's position was supported by her trustee, Mr. Paul Stehelin, Trustee in Bankruptcy with A.C. Poirier & Associates. He noted that the ten-year threshold was enacted without consultation with stakeholders – a point also made by the Canadian Federation of Students – and argued that the inability of judges to grant a discharge of student loan debt within the ten-year period in cases of exceptional circumstances is "an extraordinary provision." He, too, supported a reduction from ten years to five years and the ability of judges to discharge student debt in fewer than ten years in cases of hardship.

Mr. Stehelin also addressed the assertion that student debt should be treated differently than other debt because it is made on the "expectation of future earnings." He argued that "all of the credit card debt that students [are] granted during their student years is on the basis of an expectation of future income. … [T]here really is no difference between a student loan, a credit card or student line of credit, all of which are made on an unsecured basis and in expectation of future income."

The Canadian Federation of Students agreed that "there is no doubt that throughout the 1990s students had a more difficult time repaying their loans. … [S]tudent debt went from an average of $8,000 in 1990 to $25,000 in 1998 … . Tuition fees rose by 126% and grants were eliminated in most provinces. … The reality is that students were and are taking on huge debt to finance an education. In addition, as a needs based system, those who borrow the most are those that come to the system with the least. … [T]he social suffering this law has caused continues to mount."

The Federation also commented on other aspects of the Canada Student Loan Program. The Committee was informed that "[t]hough students are currently eligible for interest relief for a maximum of 5 years after graduation, eligibility for the program is dependent upon the loan being in good standing. … [I]f you don't miss your payments you are eligible for assistance – such a restriction ignores the reality that for those students with the highest debt, making the payments on the principal is a burden they cannot meet." It urged the federal government to repeal this "regressive legislation," and to "enact concrete solutions to address the problem of student debt. Students who borrow under the [Canada Student Loan Program] do so to finance an education and expand their ability to productively participate (sic) in society."

The Canadian Alliance of Student Associations described the requirement that individuals must wait ten years after leaving school before the discharge of their student debt as "very poor public policy" and noted the lack of public consultation before the two-year period was increased to ten years. Like most witnesses, the group recommended that the BIA be amended to permit the discharge of student loan debt five years after leaving school. It believed that such a change would strike the correct balance between "the protection of the financial sustainability of the Canada Student Loan Program and the need to treat all individuals who have fallen into serious financial misfortune in a fair and compassionate manner."

A reduction in the ten-year discharge period to five years and the possibility of a hardship hearing were supported by the Canadian Bar Association, which noted its awareness of "the hopelessness of some former students … . [The ten-year] restriction is not compatible with Canadian values of fairness and equality."

The Canadian Bankers Association advocated no change in the treatment of student loan debt, and made particular mention of the federal government's interest relief program.

The Committee believes that investing in a post-secondary education is an increasingly risky undertaking, particularly in the changing environment in which we all live. Students may invest considerable time and financial resources in a chosen course of study, only to find that upon graduation they are unable to find secure, adequately remunerated employment and in their chosen field; some are not able to find employment at all, or find themselves underemployed. As well, some may leave their post-secondary studies prior to graduation. There is, quite simply, no guarantee that the investment made in post-secondary education will yield the expected return on that investment. That being said, our future prosperity as a nation requires a highly educated and highly skilled workforce, which necessitates investments in post-secondary education.

The Committee believes that investing in a post-secondary education is an increasingly risky undertaking, particularly in the changing environment in which we all live.

At the same time, the Committee is aware that taxpayers bear a cost for student loans in a number of ways. First, taxpayers – through provincial/territorial and federal governments – pay the interest on student loans from the time when the loan is made until a certain period following graduation, at which point the student borrower begins to pay the interest. Second, taxpayers – again through provincial/territorial and federal governments – bear the costs associated with default on student loans. Moreover, loans are given without consideration of the future ability of the student borrowers to repay their student loan debt, which could be the cause of at least some defaulted loans.

From a public interest perspective, the dual goals of providing incentives for the post-secondary education needed to ensure a properly skilled and educated workforce for our future and of ensuring that taxpayers do not bear an unreasonable cost associated with government-sponsored student loans must be met. While the Committee supports the range of federal initiatives that exist to support post-secondary education, like the majority of our witnesses we believe that the ten-year period is unduly onerous and that judges must have the discretion to act in cases of exceptional circumstances. For a variety of reasons, however, including considerations related to the period of interest relief provided in the Canada Student Loan Program, we do not believe that

a two-year period is appropriate. Moreover, we are convinced that, in circumstances of undue hardship, earlier discharge is appropriate. The changes we recommend will, in our view, contribute to fairness for both students and taxpayers, and contribute to accessible post-secondary education for more of our residents. From this perspective, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to reduce, to five years following the conclusion of full- or part-time studies, the length of time prior to permitting the potential discharge of student loan debt. As well, the Act should allow the Court the discretion to confirm the discharge of all or a portion of student loan debt in a period of time shorter than five years where the debtor can establish that the burden of maintaining the liability for some or all of the student debt creates undue hardship.

I. Discharge from Bankruptcy and the Treatment of Second-Time Bankrupts

Prior to discharge from bankruptcy, a debtor's trustee in bankruptcy files a report with the Superintendent of Bankruptcy summarizing the material aspects of the bankruptcy, including the debtor's conduct during the bankruptcy and the factors contributing to his or her bankruptcy. The trustee must also report on whether the debtor has made any surplus income payments required and whether he or she could have made a viable consumer proposal.

At present, the BIA allows first-time bankrupts to receive an automatic discharge from bankruptcy nine months after filing for bankruptcy, provided that they undertake mandatory counselling and that there are no objections by creditors, the Superintendent of Bankruptcy or the trustee. When the discharge occurs, bankrupts are relieved from liability for their debts, with exceptions. Most of the non-dischargeable debts listed in the BIA have a public policy perspective that outweighs the importance of providing bankrupts with a completely fresh start following their discharge from bankruptcy. Included among non-dischargeable debts are: fines imposed in respect of an offence; debt for alimony or child support; and student loan debt, unless the bankruptcy is filed more than ten years after the debtor has left school.

At present, the BIA allows first-time bankrupts to receive an automatic discharge from bankruptcy nine months after filing for bankruptcy, provided that they undertake mandatory counselling and that there are no objections by creditors, the Superintendent of Bankruptcy or the trustee.

Creditors rarely oppose the automatic discharge from bankruptcy, although trustees may do so because of misconduct – such as failure to attend mandatory counselling sessions – or because the bankrupt has not contributed funds adequate to pay administrative costs and/or trustee fees. Where opposition to the discharge does occur, a judge or Bankruptcy Registrar will hold a hearing, and may delay or refuse the discharge; he or she may also make a conditional order requiring that the debtor make future payments.

Debtors who are bankrupt for the second time are currently not eligible for an automatic discharge. They must appear before the Court in order to seek a discharge, even when no opposition has been filed. It is estimated that about 10% of debtors filing for bankruptcy have been bankrupt on a previous occasion.

The Personal Insolvency Task Force told the Committee that "the workload of the courts remains high in many areas. … Any future increase in the number of bankruptcies would make it even more difficult for the courts to deal with discharges of bankrupts who are not eligible for an automatic discharge." It believes that the BIA should be amended to permit second-time bankrupts to be eligible for an automatic discharge 24 months after filling for bankruptcy, assuming there is no opposition; in situations of hardship, the bankrupt could apply to the Court to vary the duration of the bankruptcy. This change would "ensure that there is still a discernible and transparent consequence to individuals using the bankruptcy process for a second time." In its view, the Court should deal with discharges for third or subsequent bankruptcies on a case-by-case basis.

While the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada supported automatic discharge for second-time bankrupts, they recommended that the time period be 18 months from the date of filling for bankruptcy if more than five years have passed since the date of discharge of the previous bankruptcy; the 24-month period suggested by the Task Force should apply otherwise.

Omega One Ltd. told the Committee that the period of bankruptcy should be extended to a minimum of 15 months for all bankrupts – "if only to extend the discharge period beyond the twelve-month income tax cycle" – and for a period of 21 months for debtors who are able to make a contribution to their estates. The organization also noted that "all other countries with a bankruptcy discharge mechanism (except for

one US program) have a longer bankruptcy period than Canada." In Omega One Ltd.'s opinion, attention must be paid by legislators to "the growing misuse of the insolvency system by individuals who set out to take full advantage of a planned bankruptcy by obtaining property and cash soon before their assignment date."

The Committee believes that most bankruptcies occur as a consequence of events that are largely outside of the control of the bankrupt. While financial mismanagement may be a contributing factor, it alone is unlikely to result in bankruptcy in the absence of some other event. Given the unpredictable and uncontrollable nature of the events that may have bankruptcy as a consequence, we feel that the principle of fairness would suggest that we allow second-time bankrupts the opportunity for an automatic discharge, with the same possibility for opposition that exists for first-time bankrupts, but that their period prior to discharge from bankruptcy be relatively longer and that mandatory counselling be required. From this perspective, the Committee recommends that:

The Committee believes that most bankruptcies occur as a consequence of events that are largely outside of the control of the bankrupt.

The *Bankruptcy and Insolvency Act* be amended to provide automatic discharge from bankruptcy after 21 months for second-time bankrupts who have completed mandatory counselling. The Superintendent of Bankruptcy, the trustee or any interested party should have the opportunity to oppose the automatic discharge, in the same way that the discharge of a first-time bankrupt can be opposed, thereby requiring a Court hearing.

J. Contributions of Surplus Income to the Bankrupt's Estate

… trustees are obliged to collect a prescribed portion of the bankrupt's surplus income for the benefit of the debtor's estate and, thereby, of creditors.

Since amendments to the BIA in 1997, trustees are obliged to collect a prescribed portion of the bankrupt's surplus income for the benefit of the debtor's estate and, thereby, of creditors. In determining the amount of the surplus income, the trustee considers the bankrupt's personal and family situation, and calculates the amount of surplus income with reference to standards published by the Superintendent of Bankruptcy; these standards are based on the Low Income Cut-Offs published annually by Statistics Canada. Estimates suggest that 15-20% of bankrupts have surplus income and, as such, are required to make surplus income payments.

Trustees can recommend terms of discharge from bankruptcy that require the payment of up to 12 additional monthly payments for bankrupts with surplus income. The decision made by the trustee will be based on: whether the bankrupt has met his or her surplus income obligations during the period of bankruptcy; the amount paid to the estate in relation to total liabilities; and whether the bankrupt could have made a viable consumer proposal rather than pursue bankruptcy. This discretion allows a lack of uniformity, and could give debtors an incentive to select a trustee that is unlikely to require additional payments.

In commenting on this issue, the Personal Insolvency Task Force indicated to the Committee that "bankrupts with the financial means to contribute more to their estates should … do so, and … additional payments should be made in almost all cases for a standard 12 months." With the current nine-month period prior to discharge from bankruptcy, the result would be a duration of 21 months for bankrupts with surplus income. It believed that trustees should recommend that bankrupts with surplus income make 12 additional months of surplus income payments to their estate, and that this requirement should be included in a directive to be developed by the Superintendent of Bankruptcy, rather than included in the BIA; the directive should specify the criteria to be used in

determining the number and amount of additional payments, but should give trustees limited discretion in cases where the additional payments would create hardship.

The Task Force's proposal was supported by the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada, although they questioned whether 12 months is the appropriate length of time and expressed concern that no studies have been done to support the rationale. In their view, "[f]urther study and data are required in order to consider the number of months that may be appropriate."

In the view of Omega One Ltd., bankrupts who are able to make surplus income payments – estimated to be 15% of bankrupts – could have made a consumer proposal but, instead, selected bankruptcy; those with the financial ability to make a reasonable contribution to their creditors should be required to do so. The organization believed that "[c]onsumers who feel a need to obtain a new car, or some other desirable item, are quite prepared to commit to credit contracts lasting 36 or 48 months. It is not unreasonable to expect bankrupts who want a discharge to make (geared to income) payments for 21 months." Similarly, the Canadian Bankers Association supported allowing bankrupts with sufficient income to make reasonable contributions to their creditors.

Professors Ziegel and Telfer disagreed with those who advocated giving trustees the power to postpone a bankrupt's discharge from nine months to 21 months where he or she has surplus income.

The Union des consommateurs argued for flexibility in the formula used to calculate the surplus income. In addition to the need to make adjustments to recognize changes in the cost of living, the group suggested that there should be "some leeway … in [cases of] unforeseen events."

The Committee, in the interests of fairness and responsibility, believes that bankrupts with surplus income

… we believe that trustees should have the flexibility to modify the payments to relieve undue hardship …

should be required to make contributions to their estate that would increase the moneys available for distribution to creditors; an additional 12 months appears to be an appropriate length of time. In our view, there is some truth in the notion that these individuals could, perhaps, have made a consumer proposal that would likely involve greater recovery for creditors than is likely to be the case with bankruptcy. We also feel, however, that circumstances may arise where unforeseen events make continued surplus income payments to his or her estate difficult for a bankrupt; in these situations, we believe that trustees should have the flexibility to modify the payments to relieve undue hardship, since this too seems fair. Consequently, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to require bankrupts with surplus income to contribute to their estate for a total of 21 months. Trustees should have the discretion to permit a shorter contribution period in cases of undue hardship. Surplus income should continue to be determined in accordance with the directive of the Superintendent of Bankruptcy. The discharge of the debtor should not be delayed merely because of the obligation to continue to contribute for a total of 21 months. In appropriate circumstances, a trustee should be able to seek a summary judgment to require such payments.

K. Voluntary Agreements to Make Post-Discharge Payments

Until recently, when a filing for bankruptcy was made, a debtor and his or her trustee typically entered into an agreement providing that the debtor would make payments to his or her estate which would then be distributed to creditors in accordance with the BIA, and the payments could extend into the period after the bankrupt's discharge. Except in specific situations, the payment of trustees' fees and other administrative costs have the first claim. Trustee fees may be determined by creditors or by a tariff based on a percentage of the total value of realized assets.

A 1999 ruling held that such agreements were not enforceable, and limited the flexibility of arrangements between trustees and bankrupts regarding payment arrangements. Consequently, it was less certain that trustees would receive fair and adequate compensation for their services.

Access [to the insolvency system] is … facilitated by the OSB's Bankruptcy Assistance Program, through which trustees may voluntarily provide free services to debtors unable to afford the fees of a trustee.

The payment of trustee fees may be a barrier to access to the bankruptcy process for some debtors, since trustees who believe that it may be difficult to collect fees may require an advance or security as a condition for accepting the case. Access is, however, facilitated by the OSB's Bankruptcy Assistance Program, through which trustees may voluntarily provide free services to debtors unable to afford the fees of a trustee.

The Personal Insolvency Task Force considered a number of options for increasing the probability of adequate payment for trustees, including an across-the-board lengthening of the period before a bankrupt would be eligible for a discharge and a guarantee of compensation for services. It felt that the bankrupt's application for discharge should not be opposed by the trustee solely because of inadequate funds to pay trustee fees or the costs of administration of the bankruptcy, and that what was needed was not a guarantee of payment for trustees but rather a means by which the probability of payment was greater. In the end, it

recommended that the BIA be amended to "allow trustees to enter into voluntary payment agreements with bankrupts who do not have surplus income."

Moreover, in the Task Force's view, there should be a "ceiling on the payments made through these … agreements … related to the sum of trustees' fees and other administrative costs of the bankruptcy." Any agreement reached between the bankrupt and his or her trustee should not cause undue hardship for the bankrupt, and there should be a maximum 12-month limit on the time during which additional voluntary payments would be made. Failure by the bankrupt to sign such an agreement could result in opposition, by the trustee, to the discharge. The Task Force's views on the issue of voluntary agreements to make post-discharge payments were supported by the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada.

Omega One Ltd. told the Committee that "any agreement between the trustee and the bankrupt for the payment of scale fees and estate expenses should be deemed a non-dischargeable debt. This is the very first commitment that the bankrupt will have made to follow bankruptcy. … If the former bankrupt is allowed … to default on the very first contract he [or she] makes following bankruptcy, the rehabilitation effort is severely compromised."

Finally, Professors Ziegel and Telfer indicated that they do not support fee arrangements between a trustee and a bankrupt enforceable where the debtor's income is below Statistics Canada's Low Income Cut-Offs. They also mentioned to the Committee the Federal Insolvency Trustee Agency (FITA), through which – in the past – the federal government made low-cost bankruptcy services available through regional offices of the OSB. Although the FITA no longer exists, they recommended that it be revived in order to administer bankruptcies for insolvent persons whose income falls below the level of the Low Income Cut-Offs and who cannot afford the fees of private trustees.

The Committee believes that trustee fees may be a barrier to access for some insolvent debtors. Mindful that in Chapter Two we identified accessibility as a fundamental principle that we would like to characterize Canada's insolvency system, we believe it is appropriate that bankrupts be permitted to make an agreement with their trustees that would allow the payment of trustee fees following the discharge of the bankruptcy, with a limit placed on the amount of any such agreement. If accessibility to the insolvency system is to be a right, rather than a privilege, these agreements must be permitted. For this reason, the Committee recommends that:

If accessibility to the insolvency system is to be a right, rather than a privilege, [voluntary agreements to make post-discharge payments] must be permitted.

The *Bankruptcy and Insolvency Act* be amended to allow trustees to enter into voluntary payment agreements with bankrupts who do not have surplus income. Fees payable to the trustee in accordance with such an agreement should not exceed the minimum legal amount established for summary administration bankruptcies.

L. Non-Dischargeable Credit Card Purchases

It has been argued that – according to a practice known as "bulking up" – some debtors purposely make "luxury" or non-essential purchases on their credit cards to the maximum of their credit limit, knowing that they will soon file for bankruptcy.

Omega One Ltd. told the Committee that it routinely sees cases where credit card users appear to have "formed an intention to become bankrupt, and who use their cards to the maximum allowed just before going to see a trustee." The organization believed that Canadian insolvency legislation should include a provision providing for the non-discharge of debt that is "out of character for that particular individual." This provision would include extraordinary credit usage within a short period before bankruptcy. Similarly, the Canadian Bankers Association suggested that the BIA be amended to make luxury items purchased shortly before bankruptcy non-dischargeable.

Although the Personal Insolvency Task Force considered the issue of non-dischargeable credit card purchases, it argued that this behaviour could best be addressed by the Court on the discharge hearing of the debtor.

… in our opinion, it is not efficient to examine the credit card purchases of every credit card held by the bankrupt prior to bankruptcy with a view to identifying which purchases are "luxury" or non-essential; in any event, this determination would be subjective.

The Committee supports the view of the Personal Insolvency Task Force for a number of reasons. First, we are not convinced that the problem is so severe – in magnitude or frequency – that legislative action is appropriate. Second, in our opinion, it is not efficient to examine the credit card purchases of every credit card held by the bankrupt prior to bankruptcy with a view to identifying which purchases are "luxury" or non-essential; in any event, this determination would be subjective. Third, we support the existing availability of recourses to address these types of occurrences during the bankrupt's discharge hearing and/or by an accusation of fraud. Feeling that legislative change would not contribute to the

predictability or efficiency we believe should characterize our insolvency system, the Committee recommends that:

The matter of purchases by the debtor of luxury or non-essential goods and services shortly prior to filing for bankruptcy continue to be decided either during the course of a discharge hearing or through an accusation of fraud.

M. International Insolvency

With globalization and increased mobility of labour, there are cases in which Canadians working and living in other countries experience financial difficulties and pursue relief from creditors under the insolvency legislation in their locality.

With globalization and increased mobility of labour, there are cases in which Canadians working and living in other countries experience financial difficulties and pursue relief from creditors under the insolvency legislation in their locality. These individuals may not be entitled to pursue relief under the BIA because they may not meet Canadian jurisdictional requirements for filing, and a foreign filing may not discharge their Canadian debts without a Canadian bankruptcy filing. A foreign bankruptcy discharge does not extinguish debts governed by Canadian law; a similar situation exists with respect to a foreign reorganization order that varies or modifies debt or contracts.

If and when these insolvent debtors return to Canada, any debts incurred here before leaving the country will have survived, and only a bankruptcy filing in Canada will relieve them of these debts. In essence, they will lose their assets – and undergo rehabilitation – twice. These situations may grow in number as globalization and labour mobility continue.

The international insolvency provisions in the BIA are primarily asset-based and the definition of "debtor" is restricted to those having property in Canada, which may not be the case with a foreign-resident Canadian.

Noting that "[t]he current BIA rules … do not adequately address [the] problem," the Personal Insolvency Task Force described the current situation as inadequate and argued that the BIA should recognize the discharge or compromise of an individual's unsecured debts through a foreign bankruptcy proceeding, although with safeguards against abuse and violations of policy-based exemptions from discharge in Canada law. A second option would be extending jurisdictional requirements in the BIA so as to allow non-residents to have access to the Act's remedies.

The Task Force recommended that the BIA be amended to add a provision that would recognize the effect of a foreign discharge or compromise of debt provided that certain conditions are met. In particular, it believed that individuals should be provided with the opportunity to bring proceedings to recognize a discharge or compromise of unsecured debt granted under foreign bankruptcy proceedings. Discharge or compromise of unsecured debt effected by a foreign bankruptcy proceeding should be recognized if: there is a real and substantial connection with the foreign jurisdiction; the recognition will not violate Canadian norms of public policy; the foreign procedure was not unfair or prejudicial to creditors; and the personal exemptions used by the debtor in the foreign proceedings are substantially similar to those in Canada. No claim that survives discharge under the BIA should be extinguished by the foreign discharge. This proposal was supported by the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada, and the Canadian Bar Association also advocated the creation of a remedy for cross-border personal insolvency.

Professors Ziegel and Telfer shared a different view with the Committee. They argued that "recommendations involving the recognition of foreign personal insolvencies in Canada are both unnecessary and too complex."

Globalization and labour mobility are realities for Canada, as they are for many other countries, and are – in part – a logical consequence of some of the trade agreements that Canada negotiates. With enhanced labour mobility comes the increased possibility of international insolvency and bankruptcy by consumers having debts in more than one jurisdiction. The Committee believes in fairness and in the principle of a fresh start for bankrupts. We also support the notions of effectiveness and efficiency. All of these principles would be furthered through the development of a mechanism that would recognize insolvency filings experienced by foreign-resident Canadians, where those filings have occurred in countries that have a similar – but not necessarily identical –

With enhanced labour mobility comes an increased possibility of international insolvency and bankruptcy by consumer having debts in more than one jurisdiction.

insolvency system and approach to that which exists in Canada. We feel that foreign-resident Canadians who become bankrupt should not have to lose their assets twice, and that the Canadian insolvency system should not have to use its limited resources to duplicate a process that has already occurred in a "like-minded" country, if you will. Consequently, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to recognize the effect of a foreign discharge or compromise of debt with respect to an individual, provided certain conditions are met. The conditions should be: the bankrupt foreign-resident Canadian has a real and substantial connection with the foreign jurisdiction; the foreign procedure is fair and non-prejudicial to creditors; and the personal exemptions used by the bankrupt foreign-resident Canadian in the foreign proceedings are substantially similar to those in Canada.

N. Debt Forgiveness by the Canada Customs and Revenue Agency

When filing for bankruptcy, a year-end date for the bankrupt is established, for income tax purposes, as the day of bankruptcy, and debt owed to the Canada Customs and Revenue Agency (CCRA) is determined by what is owed on this date. This debt is typically discharged along with other dischargeable debts.

The situation is different, however, for those who pursue the consumer proposal option. Since there is no year-end date, the CCRA holds the view that debt owed for income tax between the beginning of the calendar year and the date of the proposal is not a pre-proposal debt that can be compromised in the proposal; rather, it is a post-proposal debt that cannot be included in the proposal and consequently must be paid in full.

Since there is no year-end date, the CCRA holds the view that debt owed for income tax between the beginning of the calendar year and the date of the proposal is not a pre-proposal debt that can be compromised in the proposal; rather, it is a post-proposal debt that cannot be included in the proposal and consequently must be paid in full.

The Personal Insolvency Task Force shared with the Committee its belief that this differential treatment could create, for some insolvent debtors, an incentive to file for bankruptcy rather than to pursue a consumer proposal. In its view, "[l]ogic would dictate that provisions of the *Income Tax Act* should not encourage bankruptcies over proposals." It noted that similar incentives to pursue bankruptcy rather than reorganization are provided in the *Income Tax Act* for small business owners because of the Act's treatment of forgiven debt.

To resolve these perverse incentives, the Task Force recommended that "[f]or consumer proposals, … the year-end date for income tax purposes for individuals be the date when the proposal is filed with the Official Receiver. For commercial proposals, … the year-end date should be the earlier of (a) the date of filing of the notice of intention to file a proposal and (b) the date of filing of the proposal with the Official Receiver." Moreover, "the 'debt forgiveness' provisions found in section 80 of the *Income Tax Act* should

not be applicable to individuals who file proposals under the BIA."

The Canadian Bar Association told the Committee that, in light of the "considerable frustration with the problems presented by the discrepant tax treatment of proposals as opposed to bankruptcy," it supported the Task Force's recommendation. In the Association's view, the "discrepancy has no apparent foundation in policy" and "prevents many well-intentioned debtors from addressing their obligations through a proposal, and forces them into bankruptcy despite the clear policy goals of the BIA."

Support for the Task Force's position was also expressed by the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada, which told the Committee that "[t]he codification of a deemed tax year-end period for personal proposals would enhance ease of administration and allow for greater consistency in how these periods are treated. … By recognizing a deemed tax year-end at the date of the proposal, the tax liabilities would be clearly and easily identified within the proposal, creating certainty as to the debtor's liabilities."

The Committee believes that the insolvency system should not be structured in such a manner that debtors are provided with an incentive to pursue a filing for bankruptcy rather than a consumer proposal.

The Committee believes that the insolvency system should not be structured in such a manner that debtors are provided with an incentive to pursue a filing for bankruptcy rather than a consumer proposal. These incentives do not serve debtors well, given the social and economic costs of bankruptcy, but nor do they serve the interests of creditors, who are likely to experience a lower level of recovery with bankruptcy than they would with a consumer proposal. Believing that the tax change recommended by the Personal Insolvency Task Force would create the proper incentives and thereby contribute to fairness, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to provide that, for consumer proposals, the year-end date for income tax purposes is the date on which the proposal is filed with the Official Receiver. For commercial proposals, the year-end date should be the earlier of: the date of filing of the notice of intention to file a proposal; and the date of filing of the proposal with the Official Receiver. Moreover, the *Income Tax Act* should be amended to ensure that the debt forgiveness provisions in Section 80 of the Act are not applicable to individuals who file proposals under the *Bankruptcy and Insolvency Act*.

O. *Ipso Facto* Clauses

[Ipso facto clauses] can mean that consumers lose access to essential services and facilities, including banking and utilities.

Consumer agreements with some creditors contain a provision that permits the non-consumer party to terminate the agreement immediately in the event of the consumer's bankruptcy, even if he or she has met all obligations under the agreement. Referred to as *ipso facto* clauses, these provisions can mean that consumers lose access to essential services and facilities, including banking and utilities.

While the BIA nullifies these clauses with respect to consumer proposals, the Act's provisions do not affect the right of the non-consumer party to terminate the agreement if it is violated after a consumer proposal is filed. Moreover, the non-consumer party can apply to the Court for relief if the debtor's avoidance of the *ipso facto* clause will cause it undue hardship. The BIA does not nullify these clauses with respect to consumer bankruptcies.

Believing that there is "no good reasons why this distinction between consumer proposals and consumer bankruptcies should be maintained in the BIA," the Personal Insolvency Task Force shared with the Committee its recommendation that the BIA be amended to provide that *ipso facto* clauses can be nullified with respect to consumer bankruptcies. Avoidance of *ipso facto* clauses in contracts for the supply of utilities and other essential services was also supported by Professors Ziegel and Telfer, the Canadian Bar Association, the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada.

A different view was shared with the Committee by the Canadian Bankers Association, which "does not agree that a lender should be prevented from accelerating repayment under, and otherwise terminating, a loan agreement because the borrower is in bankruptcy." In the event of bankruptcy, the Association believed that an *ipso facto* provision should be

restricted to the ability to maintain a bank account and other basic banking services. In its opinion, the BIA should not have a provision that would prohibit *ipso facto* clauses for bankruptcy.

The Committee agrees with most of our witnesses, and believes that no distinction should be made between proposals and bankruptcies with respect to *ipso facto* clauses; to maintain otherwise would diminish consistency. Moreover, we feel that these clauses should be unenforceable in order to ensure that debtors continue to have access to the basic services that they and their families need. From this perspective, the Committee recommends that:

The Committee … believes that no distinction should be made between proposals and bankruptcies with respect to ipso facto clauses; to maintain otherwise would diminish consistency.

The *Bankruptcy and Insolvency Act* be amended to provide that *ipso facto* clauses in agreements for basic services are not enforceable with respect to consumer proposals and consumer bankruptcies.

P. Credit Reporting

Canada's credit reporting agencies assist credit grantors in their assessment of the degree of risk associated with granting credit in any particular case. This assistance takes the form of credit reports on credit applicants, who are rated using letters and numbers to describe a particular applicant's credit worthiness.

Credit reporting agencies assign bankrupts the lowest credit rating – R-9 – which may prevent them from receiving credit, although the decision to grant credit is always at the discretion of the credit grantor. This score may remain on the bankrupt's record for six years following the date of filing for bankruptcy, although it may be upgraded to R-7 two years after the debtor has successfully completed a mandatory counselling program. Since 1992, mandatory credit counselling has been required for first-time bankrupts seeking an automatic discharge from bankruptcy. With an R-7 rating, some credit grantors will once again give credit to a credit applicant.

[The situation with respect to credit rating] seems to be inconsistent with the notion that debtors should be encouraged to pursue consumer proposals rather than bankruptcy.

When consumer proposals were introduced in 1992, debtors using this option were assigned an R-9 rating for three years following the successful completion of their proposal. Since proposals often last three years, however, debtors who make successful proposals are penalized through facing an R-9 credit rating for the same length of time as bankrupts, even though their creditors recover more than would have been the case in bankruptcy. In fact, depending on the length of the proposal, it is possible that debtors with successful proposals will have an R-9 rating for a longer period of time than debtors who choose bankruptcy. This situation seems to be inconsistent with the notion that debtors should be encouraged to pursue consumer proposals rather than bankruptcy.

To rectify what it sees as an anomaly, the Personal Insolvency Task Force recommended the initiation of formal discussions between the Office of the Superintendent of

Bankruptcy, credit scoring agencies and those who use their services in order to develop "a protocol that would ensure that debtors who make successful proposals have adverse credit ratings for a shorter time than debtors who go into bankruptcy." In the event that these discussions do not bring about the desired result, the Task Force recommended that legislation be enacted to limit the extent to which a credit scoring agency can maintain an adverse credit score for a debtor who has made a successful consumer proposal; this period should be limited to no more than two-thirds of the amount of time that a bankrupt has an R-9 rating. In the event of an unsuccessful proposal, the R-9 rating would remain in force for as long as would have been the case had the debtor selected bankruptcy.

Believing that enhanced incentives to encourage debtors to undertake proposals are needed, the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada expressed their support for the Task Force proposal. They also indicated, however, that in situations where the debtor files a proposal that fails and a bankruptcy is filed shortly thereafter, "[t]he bankrupt should not be penalized for having attempted a proposal that subsequently failed." Otherwise, the debtor could have an adverse credit rating that is longer than if he or she had made an assignment in bankruptcy immediately, rather than attempting a proposal. The Canadian Bar Association also indicated its support for the Task Force proposal.

The Canadian Bankers Association shared with the Committee its belief that "debtors with successful consumer proposals should be accorded consumer reports that are less derogatory than those that go into bankruptcy … and … the rating reflected on a consumer's credit report should reflect the level of relief that they have undertaken to address their financial difficulties." In particular, it believed that "[f]ull bankruptcy should receive an R-9 rating for the full seven years, a consumer proposal should receive a less derogatory rating for a lesser time period, and a consumer that has fulfilled an orderly payment of debt program or debt management program from a credit counselling (sic) should

receive an even less derogatory rating for less time than the previous two options." Similarly, in the view of Omega One Ltd., "[c]onsumer [p]roposal debtors should be accorded consumer (credit) reports that are less derogatory than those for bankrupt consumers."

The Canadian Bankers Association believed that this treatment of ratings would give consumers an incentive to enter into a credit counselling proposal before filing for bankruptcy. The Association also told the Committee that decisions about the credit rating assigned to debtors with successful consumer proposals should be left to negotiations between credit bureaus and provincial/territorial governments, and not addressed through legislation.

At the very least, we should not permit legislative, administrative and procedural measures to give debtors an incentive to choose bankruptcy rather than a consumer proposal.

In the Committee's view, debtors should have appropriate incentives to pursue consumer proposals, when that is preferable to bankruptcy for them. At the very least, we should not permit legislative, administrative and procedural measures to give debtors an incentive to choose bankruptcy rather than a consumer proposal. We believe that successful proposals represent a win-win situation: the debtor does not become bankrupt and presumably is better able to attain credit in the future, and creditors are likely to recover greater moneys than would be the case if the debtor became bankrupt.

The Committee does not, however, believe that credit rating agencies should be statutorily compelled to implement a strict regime with designated ratings for bankrupts, debtors who have made a successful consumer proposal and debtors who have made a consumer proposal that has not succeeded. In the interests of fairness for debtors, credit grantors, credit rating agencies and other stakeholders, we are wary of federal legislative intervention in this area and we are concerned that constitutional issues with respect to property and civil rights might well arise. Nevertheless, the Committee feels that the current credit rating system contains perverse elements and does not reward efforts by insolvent debtors to honour a greater portion of their obligations than would be the case if

such debtors were to go into bankruptcy. In some sense, fairness is lacking. As a result, the Committee recommends that:

The Office of the Superintendent of Bankruptcy take a leadership role in convening a meeting among credit granting agencies, credit grantors, provincial/territorial representatives and other relevant parties with a view to negotiating a mutually acceptable credit scoring regime.

Q. Inadvertent Discharge of Selected Claims in Proposals

Section 178 addresses, among others, those holding claims for: support arrears; fraud or misrepresentation; a restitution order; or damages for intentional bodily harm.

The BIA provides that if a consumer proposal or a commercial reorganization is accepted by creditors and approved by the Court, it is binding on creditors in respect of all unsecured claims, but it does not release the insolvent debtor from the debts and liabilities referred to in Section 178 of the Act, unless the creditor agrees. Section 178 addresses, among others, those holding claims for: support arrears; fraud or misrepresentation; a restitution order; or damages for intentional bodily harm. Consequently, with the agreement of the holder of a claim, debts and liabilities in Section 178 may be released, and agreement will end non-dischargeable pre-proposal claims other than those paid through the proposal.

The Personal Insolvency Task Force believed that there is a technical problem with the BIA in connection with the discharge of Section 178 claims in proposals. It raised the question of the meaning of "assent," and argued that the Court has not historically interpreted the provision to require, for Section 178 claims to be ended, the claimant to specifically agree to waive Section 178 protection.

The Task Force believed that "[i]t was definitely not the intention of the 1997 BIA support amendments to prohibit or deter support claimants from participating in bankruptcy proposals" and that "[b]ecause of the important public policy reasons that underlie the Section 178 exceptions to discharge, and particularly those relating to support, it is essential to protect such creditors from unknowing or inadvertent extinction of their claims through otherwise responsible conduct." It suggested that the BIA should be amended to revise and clarify these provisions to provide that Section 178 protection is lost in a proposal only if the creditor votes in favour of a proposal which specifically and explicitly provides for the compromise of Section 178 claims. The Task Force's position was supported by the Canadian Bar Association.

The Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada, however, shared with the Committee their view that the options considered by the Task Force are too limited. They believed that the BIA should be amended so that, in the absence of an affirmative and informed consent by each Section 178 claimant, all Section 178 claims in proposals should survive discharge from bankruptcy. In their opinion, "[t]he public policy objective of Section 178 is that certain debts are not discharged in bankruptcy because of their special nature, including court imposed monetary fines, awards for bodily harm, spousal support, child support, fraud and student loans. The nature of these claims is such that, on balance, the survival of the claim outweighs the possible benefit in the bankrupt being relieved of them. There should not be any differentiation among creditors covered under Section 178."

Many of these [Section 178] claims, by their very nature, are instrumental to the mental and/or physical health and well-being of groups in society that might be considered relatively vulnerable.

The Committee unequivocally supports the general opinion of the witnesses that the BIA must be amended to ensure that the holders of Section 178 claims do not inadvertently or innocently extinguish their rights. Many of these claims, by their very nature, are instrumental to the mental and/or physical health and well-being of groups in society that might be considered relatively vulnerable.

The Committee agrees with the assertion that, in order for Section 178 claims to be ended, those holding the claims must explicitly agree to their termination; termination must not occur because of confusion among stakeholders about what "assent" means and whether the holder of a claim has "assented" to its termination. The law needs absolute clarity in this area, given the particular importance of many of the Section 178 claims. Consequently, believing that fairness must be enhanced, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to ensure that an insolvent debtor will not be released from the debts and liabilities referred to in Section 178 unless the holder of those debts provides affirmative and informed consent.

R. Bankruptcy and Family Law

In 1997, the BIA was amended to provide for the provability and limited priority for child and spousal support arrears, thereby resulting – in some cases – in the payment of a dividend to the claimant spouse for the arrears where no payment had before existed in the event of the non-claimant spouse's bankruptcy. Unpaid remaining claims for support arrears, however, survive discharge from bankruptcy. The Office of the Superintendent of Bankruptcy receives a 5% levy on these dividends, as it does in all cases where dividends are paid by trustees to creditors. A Court decision has confirmed that the claimant spouse cannot recover the amount of the levy.

Recognizing the "special vulnerability of support claimants" and "public policy favouring the collection and payment of spousal and especially child support," Mr. Robert Klotz, of Klotz Associates, recommended that the BIA be amended to ensure that bankruptcy does not prevent support claimants from recovering the total amount of their support arrears from the bankrupt spouse. In his view, the burden of the levy should be borne by the individual paying support, rather than by the recipient of the support payments; otherwise, the support claimant "would suffer from the bankrupt's choice to declare bankruptcy." He believed that this provision should apply with respect to all Section 178 creditors, but particularly those with claims for support arrears.

In theory, the bankrupt should make surplus income payments to his or her trustee, for disbursement to creditors, only if there are sufficient moneys available after meeting the reasonable financial needs of his or her family; for a separated family, this should include support obligations.

In theory, the bankrupt should make surplus income payments to his or her trustee, for disbursement to creditors, only if there are sufficient moneys available after meeting the reasonable financial needs of his or her family; for a separated family, this should include support obligations.

Under Section 68 of the Act, the trustee and the Court are required to have regard to the personal and family situation of the bankrupt, and the Superintendent of Bankruptcy's surplus income standards require that the trustee permit the

bankrupt to deduct both child and spousal support payments in the calculation of surplus income. Section 69.41(2)(b) of the Act, however, provides that the enforcement of support claims is stayed against "amounts that are payable to the estate of the bankrupt under s. 68." In some cases, this provision has been interpreted as allowing the trustee to enforce this obligation in priority over the support claimant's wage garnishment once a surplus payment agreement has been made.

Mr. Klotz informed the Committee that, because of the interaction among Section 68 and Section 69.41 of the BIA and the Superintendent's surplus income standards, difficulty is being created for spouses who attempt to collect support from the wages of a bankrupt spouse when that spouse has entered into a surplus income agreement with his or her trustee. To correct the ambiguity that has been created, he recommended that the BIA be amended to clarify that only Court orders made under Section 68 of the Act have priority over the enforcement of spousal and child support against the bankrupt's income during bankruptcy. He believed that agreements made between the bankrupt and the trustee should not have priority over support obligations.

A third issue to be considered with respect to family law and insolvency is the extent to which bankruptcy may be used to frustrate division of the bankrupt's pension and such other exempt assets as life insurance Registered Retirement Savings Plans (RRSPs).

The Committee was told by Mr. Klotz that "[t]here is no policy reason for permitting bankruptcy, which does not distribute [pension and life insurance RRSPs] among creditors, to frustrate the principles of matrimonial property division against these assets. [Allowing this to occur] would amount to rehabilitating the bankrupt at the expense of his or her spouse."

In Mr. Klotz's view, an amendment is needed to the BIA in order to provide that bankruptcy does not stay or release any claim for equalization or division against exempt

assets under provincial/territorial legislation in the areas of equalization and/or division of matrimonial property.

In some provinces/territories and in certain circumstances, the trustee acquires the right of the bankrupt to sue the non-bankrupt spouse for matrimonial property division or equalization. This right is treated as an asset that vests with the trustee, although the matrimonial property claim is generally not a valuable right in the hands of the trustee.

Mr. Klotz believed that "one cannot reliably bring this kind of claim to fruition when it has been detached from the spouse for whose benefit the remedy was designed. … [E]ven if the right to sue for equalization or division accrues to the trustee, the sad fact is that the trustee is rarely in a position to realize upon this asset in any meaningful way. It must usually be settled for a steep discount, or surrendered for nothing." Confidence in the system is thereby undermined, since: the bankrupt spouse is denied the opportunity to obtain matrimonial justice; the non-bankrupt spouse retains most of the bankrupt spouse's share of the family assets; the creditors receive very little; and the bankrupt spouse cannot trade his or her equalization claim for reduced spousal or child support. He supported an amendment to the BIA that would exclude, from the assets vesting in the trustee, the right to sue the bankrupt's spouse for equalization or division of property under provincial/territorial matrimonial property law.

In some cases of marital discord, bankruptcy is used by a spouse as a means to ensure that the other spouse receives nothing when the marital assets are divided.

A final issue to be considered is malicious or fraudulent dissipation or concealment of property. In some cases of marital discord, bankruptcy is used by a spouse as a means to ensure that the other spouse receives nothing when the marital assets are divided. Other means that might be used by the spouse include: deception; dissipation; concealment; destruction of property; phony creditors; fraudulent transfers; and corporate machinations. A problem arises, however, in proving the allegation that the spouse acted in this way. While there are mechanisms for addressing this problem in cases of

bankruptcy, opposition to the bankruptcy discharge hearing is useful only if the other creditors are limited.

The Committee was also told by Mr. Klotz that "[i]f we are to take seriously the injustice created by such conduct, we ought to provide a simple remedy to the victim, if we can, that does not embroil him or her in a fresh round of litigation once bankruptcy ensues. At the same time, we must be concerned that this remedy is appropriately designed so as not to prejudice an honest but unfortunate debtor."

Mr. Klotz suggested to the Committee that the BIA be amended to exclude, from a discharge from bankruptcy, any provable claim for matrimonial property division that arises from the bankrupt's malicious or fraudulent dissipation or concealment of property. This exclusion should be limited to the amount of the dividend that the creditor would have received had the conduct not occurred. In particular, he believed that Section 178 of the BIA should be amended to add, to the debts that survive bankruptcy, a debt for equalization or division of property under provincial/territorial matrimonial property law, to the extent that the debt arises from malicious or fraudulent dissipation or concealment of property by the bankrupt.

The Committee endorses the recommendations and reasoning provided by Mr. Klotz. We are concerned about the manner in which a law – and interaction between laws – can have unintended consequences that negatively affect innocent individuals. The issues raised by him require prompt resolution. We must ensure that the devastating effects of marital breakdown and its aftermath are, to the extent possible, minimized – financially and otherwise – for all parties concerned, but particularly for those who are blameless. We are concerned, as well, about the fact that the Crown may receive any moneys owed in priority to child support and alimony payments. Clearly, the changes that Mr. Klotz proposed support our fundamental principles of fairness and responsibility. From this perspective, the Committee recommends that:

We must ensure that the devastating effects of marital breakdown and its aftermath are, to the extent possible, minimized – financially and otherwise – for all parties concerned, but particularly for those who are blameless.

The *Bankruptcy and Insolvency Act* be amended to:

- **ensure that bankruptcy does not prevent a claimant from recovering the total amount of support arrears from a bankrupt spouse;**

- **clarify that only Court orders made under Section 68 of the Act have priority over enforcement of spousal and child support against the bankrupt's income during the period of bankruptcy;**

- **provide that bankruptcy does not stay or release any claim for equalization or division against exempt assets under provincial/territorial legislation regarding equalization and/or the division of marital property;**

- **exclude, from assets vesting in the trustee, the right to sue the bankrupt's spouse for equalization or division of property under provincial/territorial matrimonial property law; and**

- **add, to the debts that survive bankruptcy, a debt for equalization or division of property under provincial/territorial matrimonial property law, to the extent that the debt arises from malicious or fraudulent dissipation or concealment of property by the bankrupt.**

CHAPTER FIVE: THE SENATE COMMITTEE'S EVIDENCE AND RECOMMENDATIONS ON COMMERCIAL INSOLVENCY ISSUES

A. Compensation Protection: Wages and Pensions

Under the 1949 *Bankruptcy Act*, unpaid wage claims arising during the course of an employer's bankruptcy were preferred over the claims of general creditors, to a maximum of $500. With amendments to the *Bankruptcy and Insolvency Act* (BIA) in 1992, up to $2,000 for unpaid wages, salaries and similar entitlements earned in the six months immediately preceding bankruptcy are a preferred claim; they rank ahead of ordinary creditors' claims in the event of bankruptcy but behind secured creditors' claims and some Crown claims. In particular, the claims of workers for wages and salaries rank fourth in the list of unsecured creditors having a priority of distribution, behind funeral and testamentary expenses, fees and expenses of the trustee, and legal costs. If funds are available – and often they are not – unpaid wages, salaries and similar entitlements are normally paid out some time after the date of bankruptcy.

Protection for wage earners has received a great deal of attention in Canada, having been studied by Parliament, a number of committees and others. A variety of options for protection have been proposed, including: super priority for wage claims that would rank ahead of secured claims; recognition of existing provincial/territorial priorities within the BIA regime; a waiver of the waiting period for employment insurance benefits; and a wage earner protection fund financed out of general tax revenues, or by employer and employee contributions directly or indirectly out of the employment insurance fund.

Protection for wage earners has received a great deal of attention in Canada, having been studied by Parliament, a number of committees and others.

Each of these options has advantages and disadvantages. Regarding the latter, there are concerns that a fund to which employers and employees contribute, whether through a new tax or the employment insurance system, would mean that employers with a low risk of bankruptcy, such as public service employers, would subsidize those employers with a higher risk. With a fund paid out of general tax revenues, taxpayers would finance wage protection. A super priority for wage claims would mean, in essence, that secured creditors would pay for wage earner protection.

Between the options of super priority and a wage earner protection fund – however financed – some believe that super priority status is less attractive because of: a relative lack of certainty that adequate funds will be available; the possibility of significant delay in receiving payment pending the sale of the insolvent employer's assets; difficulties associated with allocating the burden of paying claims among the secured creditors; and the creation of an unexpected burden on secured creditors and the consequent possibility of credit cost and availability problems, particularly for labour-intensive industries. It is thought that a wage earner protection fund would allow more timely payment of wages owed, thereby enabling employees to meet their most immediate financial needs pending their finding alternative employment or receiving employment insurance benefits.

The notion of a wage protection fund administered by the federal government began in 1975, when Bill C-60 proposed to implement a recommendation by the Study Committee on Bankruptcy and Insolvency Legislation – the Tassé Committee – to give super priority status to unpaid wage claims up to $2,000, binding secured and general creditors.

The notion of a wage protection fund administered by the federal government began in 1975, when Bill C-60 proposed to implement a recommendation by the Study Committee on Bankruptcy and Insolvency Legislation – the Tassé Committee – to give super priority status to unpaid wage claims up to $2,000, binding secured and general creditors. With objections raised by secured creditors, the Standing Senate Committee on Banking, Trade and Commerce recommended the creation of a federal government wage protection fund, with contributions from employers and employees used to pay outstanding employee wages to a maximum of $2,000 immediately upon bankruptcy. At the time, the Committee believed that super priority status for

wages would be detrimental to a borrower's ability to obtain financing, particularly in labour-intensive industries.

As originally introduced in 1991, Bill C-22 would have created a wage claim protection program – pursuant to the proposed Wage Claim Payment Act – financed by a payroll tax of 0.024% of an employee's weekly insurable earnings on all employers – including those in the public and quasi-public sectors whose employees would likely never benefit from the fund – to provide direct compensation to terminated employees of companies that became bankrupt, were being liquidated or were in receivership. The program envisioned payments of 90% of an employee's unpaid wages and vacation pay earned within the preceding six months, to a maximum of $2,000, and 90% of salesperson's expenses unpaid during the preceding six months, to a maximum of $1,000. The program would not have covered pension contributions, severance payments or termination pay.

Employees are seen as vulnerable creditors with inadequate individual bargaining power and a limited ability to assess accurately the risk that their employer will become bankrupt.

In May 1992, however, the Minister of Consumer and Corporate Affairs withdrew the proposed program from the Bill and in June 1992 announced the intention to refer the matter of wage claims to a Special Joint Committee of the Senate and the House of Commons for reconsideration. The Special Joint Committee, which was to have reported by June 1993, was not established. Consequently, the BIA maintains preferred creditor status for unpaid wage claims and salesperson's expenses, and the amount that can be claimed is a maximum of $2,000 for the former and $1,000 for the latter. In cases where the insolvent employer makes a proposal, these amounts are paid immediately after Court approval of the proposal. Bill C-5 did not make any changes to the amounts, although it allowed a representative of a federal or provincial/territorial ministry of labour, or a trade union, to file a claim on behalf of all employees.

Many believe that employees need better protection than that now given in the BIA. Employees are seen as vulnerable creditors with inadequate individual bargaining power and a limited ability to assess accurately the risk that their employer will become bankrupt. Whatever protection they receive – whether through super priority, a fund or

preferred claim – may have a maximum dollar amount of protection, protection related to a fixed number of pay periods and/or limitations on the compensation that is protected; some believe that protection should extend to vacation, severance and termination pay, as well as to pensions.

The Committee received a range of testimony from witnesses on the issue of unpaid compensation claims, particularly wages.

The Committee received a range of testimony from witnesses on the issue of unpaid compensation claims, particularly wages. Some supported enhanced protection, and recommended super priority status and the development of a wage protection fund. Professor Janis Sarra, of the Faculty of Law at the University of British Columbia, commented on protection for unpaid wages and on the testimony that other witnesses had presented to us. She expressed her concern "about the lobbying for a shift away from the protection of the interests of workers in the financially distressed corporation. … It seems that the discussions regarding enhanced or super-priority for wage claims and the need for a wage adjustment fund are considerably underdeveloped in the legislative review, partly because workers are disadvantaged as a group able to lobby for legislative protection." In her opinion, "[b]oth enhanced priority for workers' wages and a national wage adjustment system should be seriously considered as mechanisms to protect against unnecessary defeat of the claims of workers for compensation for services already rendered to the corporation."

Professors Ziegel and Telfer, representing a number of professors of law, also supported enhanced protection for wage earners, and expressed a preference for "a modestly enlarged Employment Insurance fund," although they also supported as an alternative solution, "a first lien against the employer's inventory and accounts receivable," particularly for a trial period to test its effectiveness. Arguing that unpaid workers are "seriously underprotected" in the existing BIA provisions, they recommended that the expanded employment insurance scheme include protection for unpaid wages, but not vacation or severance pay, up to a prescribed ceiling.

Representatives of organized labour also supported enhanced protection for the unpaid compensation of workers,

including wages but also such other elements of compensation as vacation, severance and termination entitlements, as well as pension contributions and benefits. Although speaking specifically about the *Companies' Creditors Arrangement Act* (CCAA) process, the National Automobile, Aerospace, Transportation and General Workers Union of Canada (CAW-Canada) told the Committee that "this process must recognize that workers employed by an insolvent employer have an increased vulnerability to the failure of their workplace, more so than bankers, corporate landlords, and institutional suppliers, as loss of employment may frequently mean a drastic reversal with respect to a worker's personal living conditions, and opportunities available for his/her family and community."

The United Steelworkers of America advocated both a super priority for unpaid worker claims and a wage earner protection fund, with priority for wages, vacation, severance and termination pay, and any wind-up deficiency in the pension fund. It felt that this dual protection would achieve four important objectives: the wage earner protection fund would "guarantee prompt payment of [these amounts], pending the final resolution of the issues in bankruptcy and insolvency;" it would eliminate a bias whereby severance payments for senior executives have received Court protection through the establishment of trust funds or prioritized charges; it would protect the public purse, since the sponsor/guarantor of the protection fund would assume the rights to recover some or all of the payments made by it; and it might encourage the expansion of a pension benefits guarantee fund to more jurisdictions in Canada.

The union also noted that vacation pay, pension contributions, pay in lieu of notice of termination pay and severance pay are important aspects of compensation that are compromised when an employer becomes insolvent. Moreover, among these, "an employee's severance and termination pay claim generally represents the bulk of the employee's individual claim. … The inferior ranking of employee claims must be re-visited and changed. Employees are particularly vulnerable when their employer fails, more so than a bank, landlord, commercial supplier, or other corporate

creditor. … Banks and other commercial lenders … carry a diverse range of loans. A default pertaining to one individual lending relationship should not have a material impact on the bank's prospects in the mid- to long-term. Furthermore, in the course of a banking relationship with a corporate employer, a bank has the means to analyze the risks associated with the loan in question, and manage its loan portfolio accordingly."

In the view of the United Steelworkers of America, the definition of "wages" should include termination and severance pay, and the wage priority should be increased to at least $20,000 and elevated above the claims of secured creditors. It supported an employee wage protection program that would resemble that which existed in Ontario in the early 1990s, and believed that a similar program is needed with respect to bankruptcies. A broadly based national pension benefit insurance program is also needed, in its opinion. The Canadian Labour Congress supported these proposed changes.

Furthermore, like the United Steelworkers of America, the Canadian Labour Congress noted that "[c]reditors may have a diversified portfolio of loans, and investors may be able to diversify their financial exposures, but employees have all their eggs in one basket. These circumstances create economic, legal and psychological vulnerabilities, which can easily be (and are) exploited in insolvency crises." It also told the Committee that "[t]he courts have held that 'wages' includes vacation pay but does not include pension contributions nor does it include severance and termination pay. … The Supreme Court of Canada has held in wrongful dismissal cases that because termination pay is really pay in lieu of notice it is in fact 'wages' of an employee. Accordingly, it is incongruous that the definition of wages in … the BIA excludes termination pay." In the labour federation's view, the definition of "wages" in the BIA should be amended to conform to the Supreme Court of Canada's definition of "wages", which would include termination and severance pay.

The Canadian Labour Congress also supported a federally regulated wage protection fund financed by

compulsory employer contributions based on insurable income to pay the difference between the total amount of wages owed and the amount that can be paid from the company's assets. The fund would be able to pay promptly any amounts owed to employees, beginning on the date on which payments were last made and ending on the date that insolvency proceedings were commenced. It, too, mentioned the fund that existed in Ontario in the 1990s.

[The Committee was informed about the] fund that existed in Ontario in the 1990s.

While the Canadian Bar Association acknowledged the vulnerable position of employees in insolvency situations and noted that they are economically dependent but "unable to protect themselves as adequately as creditors when an employer becomes insolvent," it told the Committee that "a super priority is neither a fair nor an efficient means of protecting the wage earner." In its opinion, a super priority would place the entire cost burden on creditors rather than spreading it amongst other interested stakeholders, particularly employers and employees, and reduce the availability of credit, among other problems. The Association expressed support for a wage protection fund under the employment insurance regime that would provide up to 90% of unpaid wages for one pay period to a maximum of $2,000. On payment to the employees, the fund would assume the rights of the employees.

Since a significant majority of its members are opposed to a comprehensive wage insurance plan that would be financed through the employment insurance fund, and consistent with its past resistance, the notion of a wage earner protection fund was opposed by the Canadian Federation of Independent Business. It told the Committee that it opposes such a fund for a number of reasons: the fund would increase the burden of payroll taxes and thereby negatively affect economic growth and job creation; from an equity perspective, well-run firms should not be required to subsidize the poor business practices of others; the BIA currently gives preferred creditor status for unpaid wage claims that meet certain criteria, and this level of protection is similar to that found in the United States; and consideration should be given to super priority for wage claims in the event that the federal

government were to determine that existing wage earner protection is inadequate.

[The Committee was told] that super priority status would not ensure the certainty or promptness of payment needed by employees.

Speaking on behalf of the banking industry, the Canadian Bankers Association expressed, as its major concern, provisions that create super priorities. In its view, the imposition of a super priority for unpaid wages would be inconsistent with the principle of efficiency, since it would impair "the ability of creditors to accurately ascertain (sic) the financial position of a borrower, … . Creditors are faced with adopting stricter lending practices because of this uncertainty, thereby limiting the availability of credit and increasing borrowing costs." It also argued that super priority status would not ensure the certainty or promptness of payment needed by employees.

The Association believed that the key issue is: who should bear the cost of providing greater protection to wage earners? In its view, "[i]t is society as a whole, and the employee specifically, that benefits from an employee receiving some compensation for unpaid wages. Therefore, either society or the employee should bear at least part of the cost of this protection. To impose this cost solely on secured creditors would be unfair and simply cause a reduction in credit availability."

Nevertheless, should the consensus be that employees require additional protection, the Association believed that the most effective method for achieving this goal is the establishment of a wage fund that would: replace a maximum of $2,000 per employee; exclude compensation for pension contributions, severance pay and termination pay; and be financed either from the Consolidated Revenue Fund, the employment insurance scheme or equal financing by employees and employers.

Finally, the Joint Task Force on Business Insolvency Law Reform provided its view that "the case for giving wage claims higher priority that they presently have has not been made. … Our proposal is for the current priorities with

respect to wage claims to be maintained, subject to clarification that pension contributions are included in wages for the purposes of the BIA."

Unpaid wages were equated with unpaid royalties by the Writers' Union of Canada, which told the Committee that authors should be treated as preferred creditors and receive their unpaid royalties *pari passu* with the unpaid wages of employees. In its opinion, such a provision should also exist in the *Canada Business Corporations Act* and similar provincial/ territorial legislation to make directors jointly and severally liable for the royalties of authors.

The Committee believes that the current protection provided by the BIA to unpaid wage claims is inadequate, and has carefully considered the views of witnesses about super priority status and a wage earner protection fund. One of our fundamental principles identified in Chapter Two – fairness – is critically important here. As we formulated our recommendation, we tried to be fair to employees, employers, creditors and taxpayers. An insolvent employer should have to bear part of the cost of protection, but so too should its employees, since they are – in some sense – creditors, having supplied services yet awaiting payment.

As we formulated our recommendation [about unpaid wage claims], we tried to be fair to employees, employers, creditors and taxpayers.

Employees are not, however, like other creditors in every respect, and thus should perhaps be protected differently. For example, they probably have a situation of economic dependence not found with other creditors, and are not well placed to assess accurately the probability that their employer will become insolvent. Fairness to taxpayers suggests that a fund financed out of the Consolidated Revenue Fund is inappropriate, while fairness to creditors means that they should not bear all of the cost of the employer's indebtedness to employees. Finally, fairness to solvent employers means that they should not have to bear the burden of costs incurred by insolvent employers. In the interest of fairness, the Committee believes that unpaid wages and vacation entitlements arising as a result of an employer's bankruptcy should be funded by a super priority over secured claims to

inventory and accounts receivable to a determined maximum amount. The secured creditors would be able to assume the rights of employees against directors. Consequently, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to provide that unpaid claims for wages and vacation pay arising as a result of an employer's bankruptcy be payable to an amount not to exceed the lesser of $2,000 or one pay period per employee claim. The funding of these claims should be assured by creating a super priority over secured claims to inventory and accounts receivable. The secured creditor or creditors should be able to assume the rights of the employees against the directors.

Another compensation issue that arises in situations of employer insolvency is protection for pension plans. While the BIA contains no provisions regarding unpaid contributions to pension plans, federal and provincial/territorial pension standards legislation provide priorities. There is, however, some question about whether priorities established in provincial/territorial legislation would be protected in bankruptcy.

Many believe that pensioners are similar to employees: they are poorly protected by current legislative provisions; they lack bargaining power; and they are relatively unable to assess accurately the risk of bankruptcy by the employer sponsoring their pension plan.

Many believe that pensioners are similar to employees: they are poorly protected by current legislative provisions; they lack bargaining power; and they are relatively unable to assess accurately the risk of bankruptcy by the employer sponsoring their pension plan. Options for protection of pensions mirror those for wages – super priority and a fund – and have similar advantages and disadvantages.

In funding pensions, there are two issues to consider: unfunded pension liabilities and unremitted periodic contributions to the pension plan. To some extent, unfunded pension liabilities should be reduced through the payments that must be made following the identification of an actuarial deficiency arising as a consequence of mandatory periodic actuarial reviews of registered pension plans.

Regarding pension protection, the Canadian Bankers Association advocated monthly employer contributions to pension plans and annual actuarial reviews of pension plans to identify any unfunded liability. In its view, if additional protection is needed for pension contributions, a fund would be the most efficient and effective method.

Organized labour also spoke to the Committee about pension protection for employees. In speaking about reorganizations under the CCAA, the CAW-Canada told us that "the CCAA should make it abundantly clear that a Court has no jurisdiction (inherent or otherwise) to interfere with the promises enshrined in a collective agreement to adequately fund (sic) for pension credits earned while the corporation carries on business under CCAA coverage, and moreover, that no pension benefit may be reduced by unilateral order of a Court. Simply put, an employer operating under CCAA coverage cannot take the continuing benefit of services rendered to it by employees but be excused by the Court from performing any one of its obligations under a collective agreement, including the funding of pensions."

The United Steelworkers of America also commented on pensions, and told the Committee that "the Courts have not been consistent in requiring that companies operating under CCAA protection continue to contribute to the pension plans of their employees. CCAA orders require that employees continue to be paid; there is no reason why the CCAA should not explicitly protect pension funds which are, after all, deferred wages." It advocated a super priority, immediately following federal and provincial/territorial taxes, for unfunded pension liabilities.

Furthermore, the Canadian Labour Congress argued that "current and future pensioners ought to be afforded maximum protection in an insolvency situation [since] of all the parties affected by an insolvency, current and future pensioners are least able to protect themselves. … [T]hey are not able to take security for future indebtedness … [and] … they are not able to impose or even bargain funding terms."

The labour federation recommended two methods of protecting pension accruals: pension insurance or the creation, under the BIA, of a super priority in cases of pension underfunding, either to overdue contributions and payments on account of the underfunding or to the overall value of the solvency deficiency at the time of windup.

For the same reasons that it did not support a super priority for employees' unpaid wages, the Canadian Bar Association also did not favour a super priority for unpaid pension contributions. Instead, it advocated protection as part of a wage earner protection fund in the event that Parliament intends to provide additional protection for these contributions.

Although the Committee recognizes the vulnerability of current pensioners, we do not believe that changes to the BIA regarding pension claims should be made at this time. Current pensioners can also access retirement benefits from the Canada/Quebec Pension Plan, and the Old Age Security and Guaranteed Income Supplement programs, and may have private savings and Registered Retirement Savings Plans that can provide income for them in retirement. The desire expressed by some of our witnesses for greater protection for pensioners and for employees currently participating in an occupational pension plan must be balanced against the interests of others. As we noted earlier, insolvency – at its essence – is characterized by insufficient assets to satisfy everyone, and choices must be made.

… insolvency – at its essence – is characterized by insufficient assets to satisfy everyone, and choices must be made.

The Committee believes that granting the pension protection sought by some of the witnesses would be sufficiently unfair to other stakeholders that we cannot recommend the changes requested. For example, we feel that super priority status could unnecessarily reduce the moneys available for distribution to creditors. In turn, credit availability and the cost of credit could be negatively affected, and all those seeking credit in Canada would be disadvantaged. Moreover, we cannot support a fund financed out of the Consolidated Revenue Fund or by employers and employees

generally, since this proposal would be unfair for taxpayers, solvent employers and the employees of these employers. In this situation, we believe that fairness is best served by the status quo. Consequently, the Committee recommends that:

[Regarding the treatment of pensions claims] we believe that fairness is best served by the status quo.

The *Bankruptcy and Insolvency Act* not be amended to alter the treatment of pension claims.

B. Debtor-in-Possession Financing

Debtor-in-Possession – or DIP – financing is a financial vehicle used to assist insolvent businesses that are restructuring. Businesses that are attempting to reorganize typically require cash, and their usual sources of credit may be unwilling to lend to them, or to lend to them at an affordable cost, because of their insolvency. Lending to these businesses is relatively risky.

With DIP financing, a new lender provides cash in exchange for a higher priority than other secured creditors; in general, existing secured creditors may not support having their security diminished by the granting of an interest to a new lender that may rank prior to, or "prime," their own. If the restructuring is not successful, the new lender is protected at the expense of other creditors, who may find their loss to be greater than if the company had instead gone bankrupt. If, however, the company reorganizes successfully, the other creditors are likely to recover more than they would have in the case of bankruptcy and job losses are reduced, with implications for employees, their families and the communities in which they live.

Some believe that new lenders should have a higher priority than other secured creditors as a premium for the risk they bear and because their financing may be instrumental to a successful reorganization.

Some believe that new lenders should have a higher priority than other secured creditors as a premium for the risk they bear and because their financing may be instrumental to a successful reorganization. The extent to which this latter point is true, however, cannot be determined statistically, since data are not systematically collected on CCAA restructurings.

While the BIA and the CCAA do not contain provisions regarding DIP financing, this financing has been authorized in CCAA cases by judges using their inherent jurisdiction. To a limited extent, the Court has allowed the security given to DIP lenders to rank prior to that of other secured creditors. Because there may be a lack of clarity about the circumstances under which DIP financing may be

authorized and the extent to which the reorganization is likely to be successful with such financing, uncertainty may prompt creditors to take action early and seize their security; there might also be implications for the availability and cost of credit.

Some believe that [DIP] financing would not be appropriate in smaller cases and would raise concerns about governance, while others feel that it should be available as a tool to enhance the possibility of a successful reorganization.

Views about whether DIP financing should be permitted in cases of BIA proposals are mixed. Some believe that such financing would not be appropriate in smaller cases and would raise concerns about governance, while others feel that it should be available as a tool to enhance the possibility of a successful reorganization.

The Joint Task Force on Business Insolvency Law Reform was among the witnesses that spoke to the Committee about DIP financing. It supported an express statutory power in CCAA cases to allow DIP loans, and told us that "it would be helpful to expressly codify the court's authority in the CCAA to give the court guidance in its consideration as to whether to grant such financing and on what basis." The Joint Task Force stressed "the link between the granting of interim financing and the governance of the corporation during the workout period," and suggested that the Court should exercise its discretion to grant DIP financing according to criteria specified in the statute. Among other considerations, it believed that the following seven factors would be appropriate:

> "(a) what arrangements have been made for the governance of the debtor during the proceedings;
>
> (b) whether management is trustworthy and competent, and has the confidence of significant creditors;
>
> (c) how long will it take to determine whether there is a going concern solution, either through a reorganization or a sale, that creates more value than liquidation;
>
> (d) whether the D.I.P. loan will enhance the prospects for a going concern solution or rehabilitation;
>
> (e) the nature and value of the assets of the debtor;

(f) whether any creditors will be materially prejudiced during that period as a result of the continued operations of the debtor; and

(g) whether the debtor has provided a detailed cash flow for at least the next 120 days."

The Canadian Bankers Association also commented on the issue of DIP financing, indicating that it is inappropriate in the context of the BIA and should be restricted on a case-by-case basis to larger companies being reorganized under the CCAA; in the latter case, the Court's authority to grant DIP financing should be codified, as should the factors to be considered in determining whether the financing should be granted. It supported some of the recommendations made by the Joint Task Force regarding DIP financing.

The Association's concern, in part, is about the effect of super priority status. In particular, it told the Committee that "[a]ny change in the negotiated priority position of a secured party will create uncertainty and limit the availability of credit. Providing for a super priority for new credit in a reorganization will have an adverse effect on pre-insolvency lending arrangements. If new and innovative companies are to receive adequate credit at reasonable costs, secured parties must be assured that their priority position will not be diminished."

In questioning the reason for allowing DIP financing to occur under the CCAA but not under the BIA and finding no policy justification for the difference, Mr. Max Mendelsohn, of Mendelsohn, G.P., told the Committee that "[i]f a reorganizing entity believes that it is too expensive to seek DIP financing in its reorganization, it will not do it or it will not be able to do it. However, it should not be denied the opportunity to try to do it if the concept makes sense."

This sentiment was supported by the Canadian Bar Association, which argued that "the same factors that lead to the need for DIP financing in a CCAA reorganization also

exist in BIA proposals." It recommended that DIP financing be available on a consistent basis in both BIA proposals and CCAA reorganizations. Since the granting of DIP financing affects the interests of stakeholders, the Association also told the Committee that the debtor should have the burden of proof on application for DIP financing.

The Committee believes that Debtor-in-Possession financing may be instrumental in ensuring the continued operation of businesses during restructuring, but cautions that reorganization may not be the preferred solution in all cases, since there may be instances where liquidation is the option that, in the long run, will be best for all stakeholders.

That being said, if DIP financing is to be used, the Committee believes that the Court should be provided with some guidance in deciding whether to approve this financing, and that it should – in the interests of fairness – be available in both CCAA reorganizations and BIA proposals; some proposals can be relatively significant in their size and scope. In our view, the entity providing the financing should be compensated for the risk that it is taking, but existing secured creditors should receive notice that the Court is contemplating the approval of DIP financing and a DIP lien that would have priority over their interests. The availability of DIP financing, criteria to guide the Court's decision making, notice to secured creditors and priority for DIP lenders would help to meet several of the fundamental principles identified by us in Chapter Two, including fairness, predictability and efficiency. For these reasons, the Committee recommends that:

… if DIP financing is to be used, the Committee believes that the Court should be provided with some guidance in deciding whether to approve this financing, and that it should – in the interests of fairness – be available in both CCAA reorganizations and BIA proposals; some proposals can be relatively significant in their size and scope.

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit Debtor-in-Possession financing. The Court should be given the jurisdiction to provide that the lien by the Debtor-in-Possession lender can rank prior to such other existing security interests as it may specify. As well, any secured creditor affected by such priority should be given notice of the Court hearing intended to authorize the creation of security ranking prior to its security. In deciding whether to

authorize a Debtor-in-Possession loan, the Court should be required to consider the seven factors outlined by the Joint Task Force on Business Insolvency Law Reform in its March 2002 report.

C. The Rights of Unpaid Suppliers

Unpaid suppliers were first given protection in the BIA in 1992, when they were provided with the right to repossess merchandise delivered to a purchaser who goes bankrupt or goes into receivership, although a number of conditions apply …

The notion of protection for unpaid suppliers when a purchaser goes bankrupt is not new in Canada. A provision in this regard was found in Quebec's *Civil Code* and was proposed in the *Report of the Study Committee on Bankruptcy and Insolvency Legislation* – the Tassé Report – in 1970. Unpaid suppliers were first given protection in the BIA in 1992, when they were provided with the right to repossess merchandise delivered to a purchaser who goes bankrupt or goes into receivership, although a number of conditions apply:

- the supplier must make a written demand for the goods within 30 days after delivery;
- the purchaser must be bankrupt or in receivership when the demand is made;
- the goods must be in the possession of the receiver, trustee or purchaser;
- the goods must be identifiable and not fully paid for; and
- the goods must be in the same state as they were on delivery and not resold at arm's length or subject to an agreement for sale.

When the purchaser has made partial payment for the goods, the supplier may repossess a portion of the goods that is proportional to the amount owing; alternatively, he or she may repossess all of the goods after repaying any partial payment received. While the right to repossess does not extend to situations where the company is reorganizing under the BIA, if the company subsequently becomes bankrupt the supplier may exercise its right to repossess goods delivered just prior to reorganization, provided the 30-day period has not expired.

Special rights exist for farmers, fishers and aquaculturalists who deliver their products to a purchaser who

subsequently becomes bankrupt or is placed in receivership. Where these products are delivered within 15 days prior to the bankruptcy or receivership and the farmer, fisher or aquaculturalist files a claim for any unpaid amount in respect of them within 30 days thereafter, the claim is secured by a charge on all inventory held by the purchaser and takes priority over all other rights or charges against that inventory except a specific unpaid supplier's right of possession.

The "30-day goods rule" was introduced to protect suppliers – who often lack a realistic ability to demand security for the transaction – from harm by insolvent debtors who order excessive amounts of inventory prior to bankruptcy as a means of increasing the assets available to satisfy secured creditors, a practice that is sometimes referred to as "juicing the trades."

The "30-day goods rule" was introduced to protect suppliers – who often lack a realistic ability to demand security for the transaction – from harm by insolvent debtors who order excessive amounts of inventory prior to bankruptcy as a means of increasing the assets available to satisfy secured creditors, a practice that is sometimes referred to as "juicing the trades." It also, however, can assist businesses in financial difficulty; because suppliers can recover their goods under certain circumstances, they may be willing to continue supplying to these businesses.

There is some controversy about the effectiveness of the 30-day goods recourse and about whether it should exist at all. While suppliers support the concept of protecting trade creditors, there are some criticisms. For example, the time frame within which unpaid suppliers must act to preserve their right to repossess often bears no relationship to the date of the purchaser's bankruptcy, which is the event that prompts repossession. When a purchaser goes bankrupt near the end of the 30-day delivery period, it may be difficult – if not impossible – for the unpaid supplier to receive notice of the bankruptcy and to deliver the repossession demand before the period expires. Effective exercise of the right may require advance knowledge about the impending bankruptcy.

A second problem concerns the requirement that the goods be in the same state as they were on delivery; any transformation through a production process means that the repossession right ceases to exist. Problems also arise where the goods are sold prior to the unpaid supplier making a claim for repossession. Moreover, the protection is limited to suppliers of goods, since those who supply services and credit

have no protection, and to situations of bankruptcy, since no protection is given by either the BIA or the CCAA in situations of reorganization. Some debtors have, for example, liquidated assets during the period of the stay of proceedings that occurs with the filing of a notice of intention to make a proposal, and have paid other creditors from the proceeds of the sale of these goods.

Supplier repossession reduces the assets in the bankrupt's estate and, consequently, the moneys available for distribution to creditors. As a result, credit availability and cost could be affected. In some sense, other creditors bear the cost of protection for the suppliers of 30-day goods. Moreover, the ability to repossess gives the supplier a right that was not part of the contract negotiated between it and the company; the argument may be made that if the supplier wanted to obtain security, this protection could have been available through the negotiation of the contract.

Supplier repossession reduces the assets in the bankrupt's estate and, consequently, the moneys available for distribution to creditors.

Witnesses shared with the Committee a variety of views about the 30-day goods rule, with some suggesting that it be abolished for the reasons cited above, and others recommending that it be changed to correct the deficiencies that have been identified. The Joint Task Force on Business Insolvency Law Reform told the Committee that "there is no justification for preferring suppliers over other unsecured creditors. … In our view, there is no case for increasing further the protection of unpaid suppliers in bankruptcy. On the contrary, there is a strong case for removing the special preference for suppliers of goods altogether."

Mr. Andrew Kent, of McMillan Binch LLP, expressed support for the position of the Joint Task Force that the claim should be eliminated. In his view, if the law were to be amended to give enhanced status to the claims of suppliers of 30-day goods, then the business would have no bargaining leverage with the supplier. He also believed that suppliers already have a number of tools that they can use to protect themselves, and are making "a conscious business choice" if they fail to do so.

[The Committee was told that giving suppliers more rights] … could undermine restructuring efforts in cases where compromising supplier claims is required.

Mr. Kent also provided the Committee with a third reason for not providing enhanced status to suppliers. Describing the situation as a "pure special interest group grab," he suggested that there is no policy justification for favouring this group and noted that many of the beneficiaries would be large, foreign companies. According to him, "pandering to special interest groups without good policy justification will make [Canada] less competitive and hurt all of us." He also opposed suppliers being given more rights in restructuring proceedings, which could undermine restructuring efforts in cases where compromising supplier claims is required.

In support of Mr. Kent's position, the Canadian Bankers Association advocated repeal of the relevant sections of the BIA. In its view, the rights for unpaid suppliers have a number of consequences; in particular, their existence: limits the availability of operating credit; adds to the monitoring cost of creditors which, in turn, results in higher interest rates; adds to the costs of debtors, who need to provide more detailed inventory accounting; duplicates existing supplier protection mechanisms; and may promote lax credit granting practices on the part of suppliers. At a minimum, the Association opposed any enhancement to unpaid supplier protection in the form of a super priority.

The Canadian Bar Association described the protection for unpaid suppliers as "difficult to apply in practice" and "largely illusory." Among the problems identified by the Association were the timing of commencement of the 30-day period and its lack of application to suppliers of services or of credit. In its view, if Parliament wishes to retain the provision, the notice should be given to the trustee within 15 days of the effective date of bankruptcy/receivership for goods delivered in the 30 days prior to the bankruptcy/receivership.

Other witnesses supported statutory protection for unpaid suppliers. The Canadian Federation of Independent Business described some of the challenges faced by small businesses that supply goods to firms that become bankrupt. For example, since customers generally have 30 days in order to pay for their goods, the last day on which goods could be

seized is the same day that the invoice is due to be paid. As well, since goods must be in the same state as when they were delivered, slight alteration of the goods or simply opening the box may preclude repossession by the unpaid supplier. Third, some small and medium-sized businesses have encountered debtors that "load up" on goods on credit before initiating bankruptcy proceedings; this action has the effect of increasing the asset base, and thus recovery by secured creditors, at the expense of the unpaid suppliers. Moreover, small and medium-sized businesses are concerned about "quick flips," whereby a company enters receivership, does not pay unsecured creditors, and begins operations shortly thereafter under a new name but with the same assets and management structure.

The Federation provided the Committee with a number of recommendations for change that would provide unpaid suppliers with relatively more effective protection: the repossession right should be extended beyond 30 days; the rules should be clarified and made fairer for unsecured creditors; ownership of goods purchased on credit should not pass to the debtor until the goods are paid in full; unpaid suppliers should be represented on a creditors' committee that would help to oversee the bankruptcy process; the debtor should be at arm's length from the disposal of assets; and rules regarding asset rollovers should be tightened, with more severe penalties to prevent abuse.

Professors Ziegel and Telfer urged improved protection for unpaid suppliers of goods and argued that the "seller's right of repossession should be converted to a lien right where the debtor has initiated reorganizational proceedings under the BIA or the CCAA."

Equifax Canada Inc. argued that "[t]he … 30-days goods rights … have not provided satisfactory protections … . [A] reorganizing business can invariably stave off the statutory claims of unpaid suppliers until the goods in question have been consumed in the manufacturing process or have

otherwise become unavailable for recovery under the restrictive terms of the BIA."

The Writers' Union of Canada also commented on the issue, and told the Committee that while authors "do not own the physical copies of their works, [they] should be treated in a manner akin to the treatment of unpaid suppliers to repossess their goods proportional (sic) to unpaid amounts. … A publisher's 'goods' … include the intellectual property. If that intellectual property has not been fully paid for, the author should have a lien on the physical books to the extent of the accrued royalties or other shortfall in payment." The Union would like to have rights comparable to those given to farmers, fishers and aquaculturalists in the BIA.

The Committee, on balance, believes that the current provisions [with respect to unpaid supplier rights] in the BIA are not working as they were intended.

The Committee, on balance, believes that the current provisions in the BIA are not working as they were intended. According to a recent Court judgment, when abuses such as "loading up" or "quick flips" take place, creditors who are prejudiced have recourse against the directors and/or management of the offending debtor. Like our witnesses, we believe that there is a myriad of problems with the 30-day goods rule, with the consequence that the protection has no practical value. The question then to be decided is: should we recommend improvements to the existing provisions, or should we recommend that the provisions be repealed? We received much testimony to suggest that the existing provisions are not effective; moreover, they are not accessible to all suppliers – being limited to goods and to situations of bankruptcy – and are not fair from the perspective that they provide protection to recent unpaid suppliers at the expense of other creditors. Clearly, a number of the fundamental principles identified by us in Chapter Two are not being served by the current provisions. We believe that the appropriate action is their repeal, rather than their amendment, with the exception of farmers, fishers and aquaculturalists for whom the provisions remain appropriate. For this reason, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to repeal, subject to the noted exception, the provisions that provide protection for unpaid suppliers of goods to bankrupt companies. The provisions that protect the rights of farmers, fishers and aquaculturalists as suppliers should be retained.

D. Cross-Border Insolvencies

… it is important that the legal approaches to insolvency in the affected countries be adequate and harmonious in order to facilitate the recovery of financially troubled businesses if that is possible and desirable, to ensure the equitable sharing of the loss if it is not and, most generally, to ensure a fair, efficient and predictable administration of cross-border insolvencies in order to safeguard capital flows and international investment.

Canadian insolvency legislation is designed to address domestic corporate failures. With the globalization of international markets and businesses, however, there are increasing numbers of insolvencies that are international – or cross-border – in nature. From this perspective, it is important that the legal approaches to insolvency in the affected countries be adequate and harmonious in order to facilitate the recovery of financially troubled businesses if that is possible and desirable, to ensure the equitable sharing of the loss if it is not and, most generally, to ensure a fair, efficient and predictable administration of cross-border insolvencies in order to safeguard capital flows and international investment.

Through amendments in 1997, the BIA and the CCAA seek to harmonize Canadian bankruptcy and reorganization proceedings with those of other countries and to reduce jurisdictional conflicts that may arise when insolvencies involve assets that are located in more than one country. Despite the existence of these provisions, however, a number of the Committee's witnesses spoke about the United Nations Commission on International Trade Law (UNCITRAL) Model Law on Cross-Border Insolvency. The stated purpose of the Model Law is:

> "to provide effective mechanisms for dealing with cases of cross-border insolvency so as to promote the objectives of:
>
> - Cooperation between the Courts and other competent authorities … involved in cases of cross-border insolvency;
> - Greater legal certainty for trade and investment;
> - Fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interested persons, including the debtor;

- Protection and maximization of the value of the debtor's assets; and
- Facilitation of the rescue of financially troubled businesses, thereby protecting investment and preserving employment."

Initiated by the United Nations Commission on International Trade Law in cooperation with the International Association of Insolvency Practitioners and with the assistance of the International Bar Association, the 1997 Model Law seeks to implement a "modern, harmonized and fair framework" – respecting differences among national laws – to apply in cases where "the insolvent debtor has assets in more than one State, or where some of the creditors of the debtor are not from the State where the insolvency proceeding is taking place." More than 70 countries – including Canada – and international organizations participated in the development process, and consensus was reached on each of the Model Law's provisions.

More than 70 countries – including Canada – and international organizations participated in the development process, and consensus was reached on each of the Model Law's provisions.

In the Commission's view, while the Model Law itself envisages the possibility of modification or incomplete adoption into the system of any particular country, this flexibility should be exercised with caution, since the desired degree of harmonization and certainty across countries is diminished when changes are made, and cooperation and coordination among affected countries in any particular case of insolvency is made more difficult.

Foreign representatives would have more rights and powers regarding possession and distribution of a debtor's assets with the adoption of the Model Law than they now have under the BIA. Canadian insolvency rules, however, would continue to exist, and Canadian Courts would have the jurisdiction to require adequate protection for Canadian creditors and other interested parties.

Some of the Committee's witnesses recommended that Canada adopt the Model Law as written, while others preferred that it not be adopted and still others argued that – if adoption

is to occur – changes should first be made. In support of the adoption of the Model Law by Canada, the International Insolvency Institute informed the Committee that "[i]n a typical international insolvency, different sets of creditors assert different kinds of claims to different assets under different rules in different countries. … When insolvency or financial failure affects a multinational business, it is still most commonly dealt with through a variety of independent, separate and often-unconnected administrations, most often for different, if not conflicting, purposes." The adoption of the Model Law would help to ensure uniformity of treatment across nations.

A number of witnesses suggested that the Model Law, if adopted, should contain a reciprocity provision according to which foreign representatives could benefit from Canadian Model Law provisions only if their country has also adopted the Model Law; such a provision would, in their view, give assistance to foreign insolvency representatives that have adopted the Model Law but deny cooperation to those that have not.

[The Committee was informed that] among the countries that have considered the Model Law, only a limited number have reciprocity requirements; Canada's North American Free Trade Agreement partners are not among them.

The International Insolvency Institute indicated that, among the countries that have considered the Model Law, only a limited number have reciprocity requirements; Canada's North American Free Trade Agreement partners are not among them. In its view, "to date, the weight of international opinion seems to be against the concept of a reciprocity requirement." Moreover, "[a]dopting a reciprocity requirement would be contrary to Canada's long-standing position of leadership in international insolvency issues. It would also be inconsistent with the international insolvency provisions that were enacted … in 1997 into the BIA and the CCAA." At that time, reciprocity requirements were not considered.

Witnesses also made other suggestions. The Insolvency Institute of Canada, for example, suggested that the recognition of a foreign representative under the Model Law be conditioned by the contemporaneous appointment of a Canadian creditors' committee to safeguard the interests of Canadian creditors in a multinational reorganization or

insolvency. The International Insolvency Institute supported this view, as did the Joint Task Force on Business Insolvency Law Reform. Even though it believed that consideration should be given to retaining the current BIA and CCAA provisions, with any needed amendments, the Joint Task Force told the Committee that "if Canada does decide to adopt the Model Law, the legislation should incorporate provisions to protect the interests of Canadian creditors … . [A] Canadian creditor's (sic) committee must be appointed. … The committee would be funded out of foreign main proceedings and entitled to appoint legal counsel and financial advisers if necessary."

Mr. David Baird, Q.C., of Torys LLP, told the Committee that the introduction of the Model Law into Canada should be deferred until the resolution of a number of issues raised by him regarding the transfer of assets to a foreign jurisdiction. Should the Model Law be introduced without consideration and resolution of these issues, he believed that "as a condition precedent to any order authorizing the transfer of assets to a foreign jurisdiction, the court should be required to either appoint a creditors' committee or a licensed trustee as a monitor with such powers as may be stipulated by the court and ensure that provisions are in place to provide the creditors' committee or monitor with reasonable funding." He also recommended that select provisions in the BIA and the CCAA regarding coordination in cross-border insolvencies be amended to limit their use to the affairs of an insolvent party.

Further study was recommended by the Canadian Bankers Association, which indicated that it "would be opposed to the adoption of the Model Law if it would have an adverse effect on Canadian sovereignty." It believed that the Model Law should not be adopted until analysis has assured that it would not infringe on Canadian sovereignty or negatively affect the rights of Canadian creditors, and that it would be consistent with the structure of the Canadian insolvency system.

Professor Keith Yamauchi, with the Faculty of Law at the University of Calgary, opposed the adoption of the Model

Law. He suggested that the Model Law is probably not the best law, since "it was primarily created through the work of certain proponents who represented relatively affluent countries." In his view, "[t]he fact that Eritrea has adopted it, and certain relatively affluent countries have not, raises the concern as to whether this one-size-fits-all model will work in a major industrialized nation such as Canada." Moreover, he commented on modifications to the Model Law, suggesting that "[m]aking changes to [it] to address Canadian culture and economics goes against the urgings of [the] UNCITRAL. … I feel Canada must conduct a thorough review of the [M]odel [L]aw from a Canadian perspective to see if it adds anything to the Canadian business culture."

The Canadian Bar Association indicated that "cross-border insolvencies present unique challenges to stakeholders and to the courts in coordinating and harmonizing the administration of a liquidation or a reorganization for the benefit of stakeholders in multiple jurisdictions." In its view, "adoption of the Model Law is something to which Canada should aspire," although modifications may be needed to ensure that the interests of Canadian stakeholders are not negatively affected by foreign insolvency proceedings. Ms. Hélène Beaulieu also shared with the Committee her views about the Model Law.

We believe – as we do with respect to international trade agreements – that harmonized and predictable rules among countries with respect to insolvency will have desirable consequences for the world's nations, but more particularly for Canada: higher levels of trade, more investment and increased access to reasonably priced credit.

In the Committee's view, Canadian insolvency law must be compatible with – although not necessarily identical to – the legislation in other countries, particularly the United States which is our largest and most important trading partner and the country with which the largest proportion of cross-border bankruptcies may occur. We believe – as we do with respect to international trade agreements – that harmonized and predictable rules among countries with respect to insolvency will have desirable consequences for the world's nations, but more particularly for Canada: higher levels of trade, more investment and increased access to reasonably priced credit.

The Committee is cognizant of the leadership role Canada has had in the creation of an international insolvency law framework and in the development of the Model Law. As

well, the 1997 amendments to the BIA and the CCAA with respect to international insolvency confirm our belief that international insolvencies are occurring and require a regime within which they can be resolved. We view the adoption of the UNCITRAL Model Law as important in safeguarding the economic health of our nation and in retaining our historic leadership role. We believe, however, that reciprocity and the fair and equitable treatment of Canadian creditors in foreign proceedings are also important, particularly as a means of ensuring fairness and transparency. It is from this perspective that the Committee recommends that:

We view the adoption of the UNCITRAL Model Law as important in safeguarding the economic health of our nation and in retaining our historic leadership role.

The *Bankruptcy and Insolvency Act* be amended to incorporate the United Nations Commission on International Trade Law Model Law on Cross-Border Insolvency. Consideration should be given to adding a reciprocity provision and provisions that would assure the creation of a creditors' committee, consisting of Canadian creditors, to protect their interests. The reasonable expenses of the members of this committee should be paid by the foreign debtor, if considered appropriate by the Canadian Court.

E. Director Liability

Federal and provincial/territorial statutes expose corporate directors to personal liability for a range of corporate debts, including unpaid wages and taxes. While due diligence and/or good faith reliance defences are available in most cases, directors are subject to absolute liability for some debts, and no defence is possible. Even in the former instances, however, there is some risk.

… reduced exposure to personal liability might encourage desirable individuals to accept positions as directors.

This liability may dissuade highly competent individuals from becoming corporate directors, and from remaining with the organization during periods of financial difficulty. From this perspective, reduced exposure to personal liability might encourage desirable individuals to accept positions as directors. A high level of personal liability, however, might be supported on the basis that it should lead to highly responsible behaviour by directors in order to reduce their risks.

The subject of director liability has been examined by a federal government working group, which concluded that while their liability has increased over the 1970s and 1980s, the marketplace could address the problem and risks are manageable. In the group's view, personal liability provides directors with an incentive to perform their duties properly. The issue of director liability has also received the attention of the Standing Senate Committee on Banking, Trade and Commerce, as noted below.

Regarding sanctions for director conduct detrimental to creditors, some Courts have recently increased the responsibility of directors to consider the interests of creditors when their company becomes insolvent; in particular, they may – in appropriate circumstances – be held personally liable for failure to consider these interests.

In 1970, the *Report of the Study Committee on Bankruptcy and Insolvency Legislation* – the Tassé Report –

recommended the disqualification of directors of bankrupt companies from serving as directors and, in some situations, the imposition of personal liability on them for deficiencies in company assets. Director liability for creditors' losses was included in insolvency legislation proposed in the late 1970s and early 1980s that died on the Order Paper, and in 1986 the *Report of the Advisory Committee on Bankruptcy and Insolvency* – the Colter Report – recommended amendment of the BIA for director disqualification and personal liability for "wrongful conduct." In the 1990s, discussion has focussed on "asset rollovers," which occur when the assets of a bankrupt company are sold to its principals, usually its directors, sometimes at relatively low cost. The principals may begin operations using these low-cost assets, while creditors bear the burden of loss.

Director liability for creditors' losses was included in insolvency legislation proposed in the late 1970s and early 1980s that died on the Order Paper …

In the view of Professor Sarra, "[w]hile the good faith and duly diligent efforts of corporate directors and officers ought to be protected, a blanket safe harbour provision is likely to create *ex ante* incentives to fail to pay small trade suppliers, workers and pensioners, absent statutory language that appropriately balances these interests."

Professors Ziegel and Telfer supported the concept of a uniform provision in the BIA governing the liability of directors of an insolvent corporation for unpaid wages. They noted the liability that directors have for unpaid wages under a number of business corporations acts, and highlighted the lack of uniformity, since in some cases liability is absolute while in others a due diligence defence exists.

Regarding the personal liability of directors, the Joint Task Force on Business Insolvency Law Reform told the Committee that "independent directors [should be relieved of] personal liability for obligations arising immediately prior to a filing. Independent directors typically have little or no control over whether such obligations are satisfied and so it is not appropriate to hold them personally liable for these sums so long as the debtor files for reorganization or bankruptcy on a timely basis before there are significant arrears."

The Joint Task Force also indicated that, "in exercising their duties during the course of a reorganization proceeding, the debtor's directors and officers and the applicable insolvency administrators [should] take into account the priority of claims of different value and priority in the face of considerable uncertainty about the values of the business and the assets of the debtor." It believed that doing so "would reinforce the trend in Canadian jurisprudence toward recognizing that, in insolvency, the fiduciary duties of officers and directors include an obligation to consider the best interests of creditors as well as shareholders."

… in earlier studies this Committee has recommended measures that would limit the scope of directors' liabilities in insolvencies.

As noted above, in earlier studies this Committee has recommended measures that would limit the scope of directors' liabilities in insolvencies. Our 1996 report *Corporate Governance* recommended incorporating provisions covering directors' liability for wages into the BIA, with a due diligence defence. Furthermore, in our 1997 report on Bill C-5, we recommended legislating, in the BIA, a generally applicable due diligence defence against personal liability for directors. We continue to support this change, and believe that it is, in essence, a question of fairness and of responsibility. We also hope that such a change might have the desirable effect of increasing the number of competent individuals who wish to serve as directors, since in our June 2003 report *Navigating Through "The Perfect Storm": Safeguards to Restore Investor Confidence* we identified the concern of some about the limited pool of directors in Canada. For this reason, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to include a generally applicable due diligence defence against personal liability for directors.

F. Transfers at Undervalue and Preferences

Canada's provisions with respect to preferences – when an insolvent debtor pays one or more creditors at the expense of other creditors – have remained largely unchanged since the 1919 *Bankruptcy Act*. Provincial/territorial assignments, preferences and conveyances legislation has existed, as well, since Confederation. In 1967, a new concept was added to the *Bankruptcy Act:* that of "reviewable transaction." A reviewable transaction is a transaction between parties not dealing at arm's length where the consideration given or received – as the case may be – by the debtor is significantly greater or less – as the case may be – than fair market value. In this situation, a financial advantage is effectively conferred on the other party to the transaction, to the disadvantage of the debtor and the debtor's other creditors.

These kinds of transactions, which may occur when the debtor is insolvent or may cause the debtor's insolvency, are addressed by the law because they have the effect of reducing the moneys or assets available for distribution to other creditors. Concerns exist with respect to: difficulties that may be encountered in enforcing remedies resulting from reviewable transactions that diminish the debtor's assets; uncertainty about what transactions would, and would not, be considered to be prohibited; and the limited nature of some of the provisions, with legislation at the federal level supplemented by provincial/territorial legislation.

In particular, the provinces/territories have assignments, preferences and conveyances legislation that addresses transactions or conveyances without consideration or at undervalue. The application of this legislation, however, is not limited to situations of insolvency.

The federal legislation currently focuses on fraud and intent, which are difficult to prove.

The federal legislation currently focuses on fraud and intent, which are difficult to prove. Some have argued that it may be more appropriate to examine the result of the transaction, rather than the intent behind it. The federal

legislation is rarely used because of the difficulty, time and expense associated with it; as an alternative, the parties are more likely to access provincial/territorial legislation.

In the opinion of the Canadian Bankers Association, the current framework requires improvement. The Joint Task Force on Business Insolvency Law Reform argued for consistency between the CCAA and the BIA, and advocated "a complete code in federal insolvency law, so that there would be a national standard for challenging transactions that may affect the value of creditors' realizable claims. … Current provincial conveyances, preferences and assignments legislation … would continue to be available to creditors outside of the insolvency context."

Regarding intent, the Joint Task Force told the Committee that "[t]here is some debate as to whether the BIA should retain the current test …, which is one of establishing that the transaction was made 'with a view to' preferring a creditor, i.e. a subjective intention test. Other jurisdictions have moved away from this approach to a standard of assessing the effect of the transaction on the position of creditors with claims in bankruptcy. The difficulty is that transactions made in good faith are not necessarily protected from an 'effects-based' standard … ."

The Committee believes that there should be a uniform system nationwide for the examination of fraudulent and reviewable transactions in situations of insolvency.

The Committee believes that there should be a uniform system nationwide for the examination of fraudulent and reviewable transactions in situations of insolvency. At present, there is a lack of fairness, uniformity and predictability by virtue of both federal and provincial/territorial legislation addressing fraudulent and reviewable transactions. We feel that a national standard is needed for reviewable transactions that diminish the value of the insolvent debtor's estate and thereby reduce the value of creditors' realizable claims. Provincial/territorial legislation would continue to exist for transactions not occurring in the context of insolvency. A national system for review of such transactions would provide the fairness and predictability that we want in our insolvency system. From this perspective, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to ensure consistent and simplified rules for challenging fraudulent preferences, conveyances at undervalue and other reviewable transactions. A trustee/monitor under a proposal should have the same powers as a trustee in bankruptcy. The Acts should provide a standard for challenging transactions that may affect the value of creditors' realizable claims.

G. Bankruptcy by Securities Firms

In 1997, provisions were added to the BIA to provide a regime for bankruptcy by securities firms. Although a securities firm holds securities and cash in trust for its clients who have ownership rights in that property, the BIA's provisions provide that only "customer name securities" are to be given to the clients who own them; almost all securities and cash held by the bankrupt are pooled and distributed *pro rata* among its clients.

Since the provisions came into force, a number of bankruptcies by securities firms have highlighted ways in which the BIA's provisions might be improved. In particular, problems have been encountered with respect to mutual funds held in Registered Retirement Savings Plan accounts and whether a trustee should be permitted to liquidate a large quantity of very low-valued securities and distribute cash rather than the securities.

The Canadian Bankers Association expressed support for technical changes that would aid in the efficient distribution of assets resulting from the insolvency of a securities firm.

… it is seldom the case that legislation – particularly in a new area of application – can fully anticipate all circumstances or all unintended consequences.

The Committee is aware that the BIA's provisions with respect to bankruptcies by securities firms are relatively recent, and that certain problems have arisen as the new provisions have been applied since their enactment. In some sense, this outcome is predictable, since it is seldom the case that legislation – particularly in a new area of application – can fully anticipate all circumstances or all unintended consequences. In our view, efficiency and effectiveness require that changes be made to the BIA to resolve any problems regarding bankruptcy by securities firms that have been identified by stakeholders since 1997. Consequently, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to clarify: the definition of "net equity;" the status of cash in the accounts of bankrupt securities firms; and the applicability of Part XII of the Act to electronic transactions.

H. Financial Market Issues

When a business reorganization occurs, the automatic stay of proceedings that occurs as a consequence has been held to apply to such financial regulators as securities commissions and/or stock exchanges.

When a business reorganization occurs, the automatic stay of proceedings that occurs as a consequence has been held to apply to such financial regulators as securities commissions and/or stock exchanges. This circumstance could limit the ability of these regulators to perform their regulatory duties and take action against companies that conduct themselves improperly, which might be particularly important when there is a heightened need to control or supervise an insolvent company and thereby ensure the integrity of the country's capital markets. From this perspective, it may be appropriate to exempt financial regulators from the automatic stay of proceedings that occurs during a reorganization.

The Ontario Securities Commission (OSC) informed the Committee that it is "concerned that a court-ordered stay of proceedings under the CCAA, which extends to the actions or proceedings by a regulator, will restrict and compromise the OSC's ability to carry out its duties and mandate under the *Securities Act* to provide protection to investors and to foster the integrity of and confidence in the capital markets through enforcing compliance with Ontario securities law." It noted that other securities regulators in Canada also share this concern.

The OSC believes that the current provision in the CCAA interferes with the ability of securities regulators to exercise their statutory mandate; in particular, the OSC's mandate is to: protect investors from unfair, improper or fraudulent practices; and foster fair and efficient capital markets, and confidence in those markets. The investing public and capital market participants rely on securities regulators to carry out these types of responsibilities, and where they are restricted from doing so as a consequence of a Court-ordered stay of proceedings, faith in – and the integrity of – the system are compromised.

Consequently, the OSC proposed an amendment to the CCAA in order to exempt securities regulators from the application of a Court-ordered stay of proceedings. Such an exemption would, in its view, mirror that which is currently available for the federal Minister of Finance, the Superintendent of Financial Institutions, the Governor in Council and the Canada Deposit Insurance Corporation.

The Committee, too, is concerned about protecting investors from unfair, improper and fraudulent practices. In our June 2003 report *Navigating Through "The Perfect Storm": Safeguards to Restore Investor Confidence*, we made recommendations designed to ensure the investor confidence in publicly traded companies and capital markets that is needed for our continued economic growth and prosperity. We also believe that the amendment sought by the Ontario Securities Commission would contribute to greater effectiveness and the restored confidence we – and others – are seeking. As a result, the Committee recommends that:

The Committee, too, is concerned about protecting investors from unfair, improper and fraudulent practices.

The *Companies' Creditors Arrangement Act* be amended to give the Court the right to exempt securities regulators from Court-ordered stays of proceedings in instances where two conditions are met: the exemption is needed for the protection of third parties; and the exemption does not subject directors or senior management to undue pressure and loss of time.

The Committee also received testimony about another financial market issue: electronic money and a "partial security interest." According to van Leeuwen Engineering Limited, a partial – or shared – security interest would allow a number of creditors to share their interest in a piece of property and essentially become secured creditors; it would enable "smaller debts to be secured, which would reduce bad debt." While provincial/territorial legislative change would be required to establish the partial security interest, a federal amendment would be needed to allow "electronic money." The organization suggested that access to the Canadian Payments Association should be given so that "small start-up financial-

Believing that this proposal falls outside the scope of our review, the Committee makes no specific recommendation [about electronic money and a partial security interest].

transaction companies can plug in and try out their methodologies. If they grow, they can either eventually migrate to being a bank or … some other form of structure." The notion of a joint payment guarantee instrument was also raised.

The Committee is aware that van Leeuwen Engineering Limited has had discussions with the Bank of Canada about the proposal, and urges the organization to continue to pursue those discussions. Believing that this proposal falls outside the scope of our review, the Committee makes no specific recommendation.

I. Insolvency Practitioner Liability as a Successor Employer

At present, trustees, receivers and other insolvency practitioners may be held personally liable, as successor employers, for certain obligations of a bankrupt or insolvent debtor. While the BIA provides some protection, not all administrators have legislative protection from all claims. In particular, obligations might include wages, vacation, severance and termination pay, as well as pension claims, even where these arise prior to the appointment of the administrator. Moreover, the administrator may be unaware of the nature and scope of these obligations when he or she agrees to provide services.

If competent individuals are to become insolvency practitioners, they must be provided with some measure of protection from personal liability in their role as administrator and not be assimilated to, or treated as, successor employers. In essence, their protection must exceed the risk they assume in providing services, otherwise they are unlikely to do so.

The Canadian Bankers Association believed that there should be greater protection for insolvency practitioners against being treated as successor employers, and supported "a clear separation of the personal liability of a trustee from the liability of the debtor's estate. … [T]rustees should only be personally liable for claims occurring after their appointment, and only those that arose through their negligence."

Earlier, the Committee commented on the protection needed for directors, in part to ensure that competent individuals are willing to become directors. Similarly, we believe that insolvency practitioners need protection from personal liability, otherwise individuals are likely to be unwilling to provide these critical services. From a fairness perspective alone, it would seem reasonable to ensure that any liability they face is not the consequence of actions taken by the debtor before their appointment. For this reason, the Committee recommends that:

… *we believe that insolvency practitioners need protection from personal liability, otherwise individuals are likely to be unwilling to provide these critical services.*

The *Bankruptcy and Insolvency Act* be amended to separate clearly the personal liability of an insolvency practitioner from the liability of the debtors' estate.

J. Executory Contracts

Executory contracts are contracts under which something remains to be done by one or more of the parties to the contract. In essence, it is a contract where there are obligations yet to be completed. Examples include leases, intellectual property rights and employment contracts, among others. Neither the BIA nor the CCAA uses the expression "executory contract."

Nevertheless, the existence of these contracts in a situation of insolvency raises the question of the extent to which these private contracts – negotiated in good faith and with due consideration of risk – should be altered or terminated, under what circumstances and by whom. Alteration or termination of contractual rights change expectations, reduce predictability in contracting and increase risks, which will have negative implications. As well, both contracting parties may experience harm, since the continuation of a contract may be in the best interest of both parties.

… the existence of [executory] these contracts in a situation of insolvency raises the question of the extent to which these private contracts – negotiated in good faith and with due consideration of risk – should be altered or terminated, under what circumstances and by whom.

Canadian legislation in this area has existed for some time. The *Bankruptcy Act* passed in 1949 contained few restraints on completed contracts; as well, it explicitly recognized the applicability of provincial/territorial law to real estate leases. Various omnibus bills in the 1970s and 1980s, all of which died on the Order Paper, proposed that an insolvent person who wished to make a proposal could disclaim any executory contract, and the co-contracting party would have the right to file a claim in the proposal for damages; the insolvent company could continue as a going concern, while the co-contracting party to the disclaimed contract would be no worse off than if a bankruptcy had occurred.

Amendments to the BIA in 1992 provide that, after a reorganization begins, secured creditors cannot exercise their security; the termination of a lease, licensing agreement or public utility because of default was also prevented. Debtors, however, were given the ability to disclaim leases on real property.

Witnesses presented the Committee with divergent opinions on whether disclaimer of executory contracts should be allowed, with the Court's permission, by insolvency practitioners or by co-contracting parties. Some witnesses told us that a company involved in a reorganization should be permitted to renounce such contracts. This view was held, for example, by Mr. Mendelsohn, who told the Committee – in reference to the CCAA – that "reorganizing entities [do and should] have the ability to renounce executory contracts, … with appropriate judicial supervision." After noting that, under the BIA, only commercial leases of real estate where the reorganizing entity is the lessee can be renounced, he argued that a coherent system of restructuring must permit the entity to renounce other executory contracts as well. He informed us that "[i]f executory contracts have to be renounced, they have to be renounced whether … [the] company [is big or small]."

Mr. Mendelsohn also shared the view that a bankruptcy trustee should be able to assign and transfer executory contracts to third parties, including licensing arrangements and leases of premises. He believed that "a trustee in bankruptcy should be given the right to realize, for the benefit of creditors, whatever economic value resides in the assets, including executory contract assets."

The Joint Task Force on Business Insolvency Law Reform also spoke about the ability to disclaim executory contracts and assignment to third parties. In the Joint Task Force's opinion, "[t]here should be a general right to disclaim (reject) executory contracts (including real property leases) in all bankruptcy and reorganization proceedings." Although it does not believe that insolvent organizations or the trustee in bankruptcy should require Court approval in order to disclaim these contracts existing at the date of commencement of proceedings, the Joint Task Force argued that "the legislation could impose some pre-conditions to the exercise of the disclaimer power either generally, or with respect to certain types of contracts."

Regarding the ability to assign executory contracts, the Joint Task Force informed the Committee that "trustees in

bankruptcy and court-appointed receivers should have the power to assign executory contacts (not including eligible financial contracts) both in connection with going concern transactions and on a liquidation basis," subject to a number of limitations. It went on to note, however, that "[t]here should be provision for the court to prohibit an assignment if [the non-bankrupt party to the contract] establishes that the proposed assignee does not meet, in a material way, criteria reasonably applied by [it] before entering into similar agreements … or the proposed assignee is less creditworthy than [the bankrupt] was when the executory contract was entered into and reasonable assurances of payment have not been provided with respect to any credit required to be extended to the assignee by [the non-bankrupt party] under the executory contract after the assignment."

The Canadian Bankers Association, however, told the Committee that "[i]nsolvency law constraints on contracts can affect pre-insolvency contracting behaviour and may reduce credit availability. The new economy dictates that companies must be innovative and dynamic. In order to finance such new enterprises, financiers must be able to rely on the negotiated terms of their contracts."

A particular executory contract – a collective agreement – was discussed by several witnesses, including representatives of organized labour. In general, their view is that the Court should not be able to terminate a collective agreement, in whole or in part. The CAW-Canada told the Committee that "the CCAA offers no authority to a Court to abrogate a collective agreement. Nor should it do so. Still, some counsel and commentators believe that Superior Courts in Canada have an 'inherent jurisdiction' to issue an order pursuant to the CCAA which suspends or temporarily cancels one or more terms of a collective agreement. We fundamentally disagree."

A particular executory contract – a collective agreement – was discussed by several witnesses, including representatives of organized labour.

In the union's opinion, "[t]here can be no dispute that if the preservation of the status quo is a key objective of the CCAA, then the terms and conditions of employment defined in a collective agreement at the time of the issuance of a CCAA order must be maintained subject to the parties' mutual authority to negotiate changes." From this perspective, the

CAW-Canada told the Committee that "[t]he CCAA should … make clear that it is not open to a Court, in exercising its 'inherent jurisdiction' to alter, waive, or override the provisions of a collective agreement without the consent of the employer and the relevant trade union."

A similar view was presented to the Committee by the United Steelworkers of America, which told us that "the Courts should not be entitled, under the guise of a CCAA proceeding, to interfere with the operation of freely negotiated collective agreements which affect the rights of many workers. … [U]nions have demonstrated, in times of legitimate economic crisis, that they are capable of acting responsibly and in the best interests of their membership to agree to amendments to a collective agreement which may be necessary to enable the employer to survive. This cooperative approach is to be preferred to an approach which would eliminate workers (sic) rights with the stroke of a pen and subvert the primacy of collective bargaining."

Moreover, the Canadian Labour Congress differentiated collective agreements from other executory contracts, and indicated to the Committee that "[j]ust as employees are not like other creditors, collective agreements are not like other contracts. … [T]he bankruptcy and CCAA courts should not be accorded any jurisdiction over collective bargaining agreements. … Unlike other creditors, workers are not in a position to negotiate the terms upon which they may become creditors of their employer. Unlike other creditors, they are not in a position to assess the risks that they are required to bear. Unlike other creditors, they are not able to guarantee their employer's obligation by way of a secured charge. And unlike senior executives, they are not in a position to have their termination entitlements, including golden parachutes, set aside in trust accounts and thereby protected from bankruptcy proceedings."

The labour federation also informed the Committee that it does not support disclaimer of collective agreements. In its view, "[t]he debtor company and the union are in the best

position to evaluate the needs of the company and are also the parties with the greatest interest in preserving the company as a going concern; they are, therefore, the appropriate parties to determine any changes to the collective agreement. The key incentive for the parties to reach an agreement is the threat that a failure to do so will lead to the bankruptcy of the debtor. … Neither the courts nor the monitor or receiver should have the power to vacate or amend a collective bargaining agreement that was arrived at within the provincial or federal statutory framework." The Canadian Labour Congress, however, went farther, and argued that "the value of each concession should be assigned unsecured creditor status with no less priority of valuation than any other unsecured creditor."

In support of the views of organized labour, Professor Sara commented that "treating collective agreements as commercial executory contracts that can be unilaterally set aside … is highly problematic."

From the perspective of intellectual property rights, the Intellectual Property Institute of Canada indicated its preference for an approach that would limit the right of disclaimer to "unprofitable," rather than "executory," contracts, since there is "too much uncertainty as to what types of agreements would be found to be 'executory'." The Institute also made other suggestions for change.

For example, the Institute recommended that: the time limit for the exercise of the right of disclaimer be three months; the Court have the discretion to maintain the contract if the disclaimer would cause undue hardship not compensable in damages; the Court be permitted to make an order discharging the agreement and ordering payment for damages for non-performance by the trustee; aggrieved persons be given the status of a creditor of the bankrupt, to the extent of any loss suffered by reason of the disclaimer; and, where the bankrupt is a licensor of intellectual property rights, the licensee have the right to elect – within one month after receipt of the notice of disclaimer – to retain the licence. Recommendations were also made by it with respect to patents, trademarks and trade secrets.

[The Committee received testimony] with respect to patents, trademarks and trade secrets.

Similarly, Mr. Baird, Q.C., spoke to the Committee about intellectual property issues and noted the debate that has existed for some years about "whether a trustee in bankruptcy or a bankrupt licensor or a debtor under the protection of the CCAA has the right to repudiate licences issued by the bankrupt or the insolvent debtor." In supporting a recommendation made by the Insolvency Institute of Canada, he said that "the BIA and the CCAA [should] be amended to provide protection for a licensee of a right to intellectual property similar to that provided in the United States."

The Writers' Union of Canada also commented on copyright, noting the absence of copyright issues in the CCAA and the extent to which "the *Bankruptcy and Insolvency Act* less frequently applies – or doesn't apply initially. … When [it] does apply, it provides writers with very limited protection and often too late. A receiver or trustee in bankruptcy may already have assigned his or her rights and sold the inventory, short circuiting a possible statutory reversion of rights, depriving the author of possible revenues from sales by the trustee, and interfering with the author's future opportunities for republication." It also recommended that a trustee not be permitted to transfer or assign the copyright, or any interest in it, since the relationship between a writer and his or her publisher is personal; the writer should be permitted to make any alternative arrangements in the event of his or her publisher's insolvency. Finally, the Union commented that there is a lack of clarity about whether a publishing agreement is a partial assignment of copyright or a licensing agreement under which the author retains the copyright.

… we urge relevant parties to engage in the discussion needed to ensure a satisfactory resolution to the full range of issues identified to us by the Intellectual Property Institute of Canada.

While we believe that there are a variety of unresolved issues related to the insolvency of a licensor or a licensee in the context of an intellectual property licence, intellectual property law is a highly specialized area and we feel that the limited examination given by the Committee to this particular aspect of insolvency does not enable us to make any meaningful recommendations for change. Nevertheless, we urge relevant parties to engage in the discussion needed to ensure a satisfactory resolution to the full range of issues identified to us by the Intellectual Property Institute of Canada.

More generally, the Committee supports the concept of permitting disclaimer of all executory contracts, since we believe that the flexibility to take this action increases the probability of successful reorganization and thereby – in some sense – a fresher, if not fresh, start for the business. We also feel, however, that the parties to executory contracts should meet in good faith with a view to negotiating mutually acceptable changes to their contract that would enable them to meet their goals and permit the contract to continue, albeit in a changed form. We strongly believe that, in most cases, the parties will be able to come to a successful resolution; however, it is likely that situations will arise in which the parties cannot reach agreement, and in these cases we believe that disclaimer should be permitted by the Court. Nevertheless, disclaimer should only be allowed where certain conditions are met, including good faith attempts to negotiate mutually acceptable changes to the contract and serious hardship in restructuring without the disclaimer. Believing that this approach would enhance fairness, predictability and effectiveness, the Committee recommends that:

… the Committee supports the concept of permitting disclaimer of all executory contracts, since we believe that the flexibility to take this action increases the probability of successful reorganization and thereby – in some sense – a fresh, if not fresher, start for the business.

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit disclaimer of executory contracts in existence on the date of commencement of proceedings under the Acts. This disclaimer should apply to all executory contracts, provided a number of conditions are met. In particular: the debtor should be obliged to establish inability or serious hardship in restructuring the enterprise without the disclaimer; the co-contracting party should be permitted to file a claim in damages in the restructuring; and, where a collective agreement is being disclaimed, the debtor should also have the burden of establishing that post-filing negotiations have been carried on, in good faith, for relief of too onerous aspects of the collective agreement and should establish in Court that the disclaimer is necessary in order to allow for a viable restructuring.

Moreover, the Committee is of the view that trustees, Court-appointed receivers and monitors should be able to assign executory contracts where doing so would enhance the value of the assets and, thereby, moneys available for

distribution to creditors. We recognize that while this circumstance would not permit the co-contracting party to choose its commercial partner, we feel that if the co-contracting party is no worse off financially, it would suffer no prejudice. As well, efficiency and effectiveness – two principles that we believe should characterize our insolvency system – would be enhanced. From this perspective, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit trustees, Court-appointed receivers and monitors, if authorized by judgment, to assign executory contracts when appropriate, in connection with going concern transactions and on a liquidation basis, provided that two conditions are met: the proposed assignee is at least as credit worthy as the debtor was at the time the contract was entered into; and the proposed assignee agrees to compensate the other party for pecuniary loss resulting from the default by the debtor or give adequate assurance of prompt compensation.

K. Workers' Compensation Board Premiums

Based on a system that originated in Germany in 1884, workers' compensation is a form of insurance designed to help employees who are injured on the job or who are affected by industrial disease to receive compensation and, ideally, return to work. In essence, it represents a compromise between employers and employees; with enactment of legislation across Canada, workers gave up the right to sue their employers for injuries at work and employers agreed to contribute to a fund that finances benefits for work-related injuries and illnesses, regardless of fault.

Across Canada, workers' compensation systems generally ensure that injured workers receive: first-aid treatment on the job or at the nearest local treatment facility; benefits while recuperating from injuries; proper treatment for injuries; and, if needed, rehabilitation to help the employee return to his or her job, or to a modified job if required by the circumstances.

Prior to 1997, the BIA provided that claims of Workers' Compensation Boards were granted a priority over claims of unsecured creditors; this priority ended, however, with respect to bankruptcies occurring after 1997.

Prior to 1997, the BIA provided that claims of Workers' Compensation Boards were granted a priority over claims of unsecured creditors; this priority ended, however, with respect to bankruptcies occurring after 1997. Since that time, these claims have only been secured if a security interest was registered, or otherwise obtained, in the same manner as is available to persons other than the Crown or a workers' compensation body. As a result Workers' Compensation Board claims have, generally, been treated as unsecured claims since 1997.

The Association of Workers' Compensation Boards of Canada spoke to the Committee about the important role played by workers' compensation as "an essential component of an integrated fabric of social and economic support that is fundamental to our society." As a program of wage replacement and services, in 2001 about 374,000 Canadian workers and their families received a range of benefits from workers' compensation, including wage replacement, health care, rehabilitation services and family fatality benefits; the cost of these benefits totalled $6 billion.

The Committee was told that, prior to recent amendments to the BIA, Workers' Compensation Board premiums were considered to be deemed trusts. We were informed that, since 1996, the removal of this status has resulted in an estimated $175 million loss for Workers' Compensation Boards as workers' compensation premium claims are now treated as unsecured commercial debts. Moreover, we were told that the loss, in turn, has compromised the benefits and services that would otherwise be available to injured workers and their families. In the view of the Association, this reduced status neglects the role historically played by workers' compensation as a "public insurance program supporting the economic and social needs of injured workers and their families." In its opinion, this role differs fundamentally from that played by commercial creditors.

Consequently, the Association recommended that the *Bankruptcy and Insolvency Act* be amended to recognize Workers' Compensation Board premiums as deemed trusts, which would give them the same secured creditor priority as the Canada/Quebec Pension Plan and employment insurance premiums over lending institutions and other secured creditors. In its opinion, allowing Workers' Compensation Boards to recoup their claims in bankruptcy would affect credit costs in Canada negligibly.

The result of this change would be that, in a bankruptcy, Workers' Compensation Board claims would be superior to those in favour of a bank or other lending institution in all jurisdictions. The Association informed the Committee that this treatment would have several advantages. First, it would "[e]nsure the primacy and sustainability of [the] social-economic safety net." Workers' compensation, along with employment insurance and the Canada/Quebec Pension Plan, is "fundamental to Canadian society … [and] must be protected from revenue loss as a result of employer bankruptcy." It is a key component of the nation's social safety net and "should be recognized as a secured creditor serving the public interest rather than as another commercial creditor."

Second, while provincial/territorial legislation gives workers' compensation assessments/premiums priority in bankruptcy, the BIA does not do so and thereby "creates two different systems for distributing the debtor's assets, depending on whether or not there is formal bankruptcy;" from this perspective, amending the BIA to provide for this priority would contribute to legislative consistency across jurisdictions and support "certainty in commercial relations."

Third, priority status for workers' compensation assessments/premiums would contribute to "the fair distribution of [a] debtor's assets" since the Canada/Quebec Pension Plan, employment insurance and workers' compensation would be "equal as income security and trusts."

Fourth, returning the treatment of workers' compensation assessments/premiums in bankruptcy to their pre-1997 status would promote the "economic sustainability of workers' compensation." This sustainability is important, in the Association's view, since affordable premiums are important to help businesses constrain their labour costs and thereby enhance their competitiveness; affordability also makes Canada a more attractive country within which to invest. According to the Association, the current inability of Workers' Compensation Boards to recover moneys from insolvent companies indirectly means that premium-paying employers are paying for the bankruptcies. As well, "[u]npaid premiums result in additional costs for paying employers" as premiums rise.

Finally, in the Association's opinion, priority status for workers' compensation assessments/premiums would ensure that the proper parties bear responsibility for bad credit decisions. The Association believes that the "BIA places the burden of failed business loans on workers' compensation, not the lenders where it belongs." As a legislated program, workers' compensation is not able to choose its customer or limit its risk; Workers' Compensation Boards must recognize the claim of an injured worker regardless of his or her employer's payment of assessments/premiums, and they are unable to refuse insurance to workplaces or employers that

[The Committee was informed that] Workers' Compensation Boards must recognize the claim of an injured worker regardless of his or her employer's payment of assessments/premiums, and they are unable to refuse insurance to workplaces or employers that may have significant liabilities or that may default on assessments/premiums.

may have significant liabilities or that may default on assessments/premiums. The Association believed that banks and lending institutions, on the other hand, select their clients to manage their risk.

The Association also told the Committee that one of the goals of the BIA is not being realized with the current system. It said that "[o]ne of the goals of the BIA is the fair distribution of debtor's assets among the creditors. However, in reality, the current scheme is not fair to workers, employers and workers' compensation boards and commissions because it allows lenders to use the BIA to obtain the assets of bankruptcy thereby defeating the interests of workers, employers and workers' compensation."

In recognition of workers' compensation as an element of our social safety net, it argued that "[a]s a matter of public policy, workers' compensation should not be penalized or placed at a disadvantage in a bankruptcy proceeding. The financial stability of workers' compensation … should not be put at risk. Nor should the capacity of workers' compensation boards and commissions to meet commitments be weakened because of difficulties in recovering unpaid premiums."

The Committee was informed that, in turn, the ability of Workers' Compensation Boards to deliver benefits would be increased and workers' compensation would have the same treatment as employment insurance and the Canada/Quebec Pension Plan, which – according to the Association – likewise offer wage protection. Re-establishing this priority would reduce the extent to which Workers' Compensation Board revenues are lost to chartered banks in the event of bankruptcy.

While the Committee agrees that workers' compensation is a key component of a system designed to assist workers and their families in the event of job-related illness or injury, we are unable to support the recommendation of the Association of Workers' Compensation Boards of

Canada. In our view, the situation that existed before 1997 whereby priority over unsecured claims was granted to claims of all Workers' Compensation Boards should be reinstated. Moreover, we note that a recommendation made by us elsewhere in the report would, if adopted, import the priorities contained in the BIA into the CCAA; this change would give Workers' Compensation Board premium claims the same treatment under CCAA proceedings as under BIA proceedings. From this perspective, the Committee recommends that:

… we note that a recommendation made by us elsewhere in the report would, if adopted, import the priorities contained in the BIA into the CCAA …

The *Bankruptcy and Insolvency Act* be amended to return the treatment of Workers' Compensation Board premiums to that which existed prior to 1997.

L. Interim Receivers

Under the BIA, receivers are appointed to liquidate a debtor's assets for the benefit of secured creditors. To an increasing extent, interim receivers are being used for that purpose. There are concerns about the extent of an interim receiver's powers, the jurisdictional basis for the scope of the orders made and the impact on the rights of affected third parties in the absence of the Court determining the need for such liquidations prior to judgment.

Before 1992, the interim receiver's role was to be a "temporary watchdog" of the debtor's property, and he or she was appointed to protect the estate or the interest of creditors pending the granting of a receiving order.

Before 1992, the interim receiver's role was to be a "temporary watchdog" of the debtor's property, and he or she was appointed to protect the estate or the interest of creditors pending the granting of a receiving order. In some jurisdictions, however, interim receivership is now being used in a manner that permits the interim receiver to take possession of the debtor's assets, operate its business and, in some cases, sell assets and distribute the proceeds to secured creditors before judgment. Consequently, at times, the powers of the interim receiver closely resemble those of a trustee or Court-appointed receiver; the interim receiver has not, however, been bound by the duties and responsibilities of a trustee or receiver.

The Canadian Bar Association argued that the expanded role of some interim receivers fails to protect the debtor, ordinary creditors or affected third parties. In its view, the interim receiver's role must be more clearly defined. Moreover, the Association believed that if interim receivers play a role analogous to that of Court-appointed receivers, they should be subject to the same obligations and requirements; where their roles are the same, the definition of "receiver" should be amended to include, specifically, "interim receivers."

The Committee believes that the role of interim receivers has evolved over time, and that clarity is needed

about what should be their role, duties and responsibilities. In our view, "interim" should mean exactly that, and if a broadened or extended role is needed – or desired – then legislative change should occur in order to reflect this fact. It is, in essence, a matter of fairness and predictability, since interim receivers who act in a capacity similar to trustees or Court-appointed receivers should have not only the same powers, but also the same duties and responsibilities. Consequently, the Committee recommends that:

In our view, "interim" should mean exactly that, and if a broadened or extended role is needed – or desired – then legislative change should occur in order to reflect this fact.

The *Bankruptcy and Insolvency Act* be amended to clarify the role of the interim receiver, and the duration and meaning of the term "interim." As well, the definition of "receiver" should be amended to include interim receivers when they operate in a manner similar to Court-appointed receivers.

M. Going Concern and Asset Sales

During a reorganization, an insolvent company may benefit from an opportunity to sell part of its business in order to generate capital, avoid further diminution in value and/or focus better on the financially solvent aspects of its operations.

During a reorganization, an insolvent company may benefit from an opportunity to sell part of its business in order to generate capital, avoid further diminution in value and/or focus better on the financially solvent aspects of its operations. In some situations, a win-win situation would be created: insolvent companies would be able to increase their chance of survival as they gain capital and focus on their solvent operations, and creditors would avoid further reductions in the value of their claims. These sales would occur outside the normal course of the organization's business. In some cases, the best situation for stakeholders might involve the sale of the business in its entirety.

At present, the Court exercises its inherent jurisdiction in approving these asset sales. It does so, however, without any legislative guidance about when and how such sales should occur.

The Joint Task Force on Business Insolvency Law Reform told the Committee that "[i]n practice, successful restructurings usually require much more than simply obtaining financial concessions from existing creditors. They usually involve an operational restructuring of the business as well as a financial restructuring. … The debtor may need to sell or shut down parts of its business, either to generate new capital or to withdraw from the financially unhealthy parts of its business in order to save the financially sound parts. … In some situations, the economic and social objectives of the insolvency system can be better achieved through a sale of the debtor's business as a going concern to a new owner, rather than through the restructuring of the legal entity that is the current owner."

The Joint Task Force provided the Committee with a non-exhaustive list of guidelines that it believed would give the Court "substantive direction" regarding factors to consider in deciding whether to approve a sale of assets – in whole or in part – on a going concern basis during a CCAA proceeding.

In particular, it suggested that the Court might assess whether the sales process has been conducted:

> "(a) in a fair and reasonable manner;
>
> (b) by an insolvency administrator;
>
> (c) by a credible, independent chief restructuring officer reporting to a credible, independent restructuring committee of the board of directors either with or without supervision of the court; and/or
>
> (d) in consultation with major creditors."

When the debtor – instead of being reorganized under the CCAA – has made a proposal under the BIA, the Joint Task Force indicated that there may not be a restructuring officer or a restructuring committee. In that case, input should be sought and obtained from major creditors, as is envisaged with respect to reorganizations under the CCAA, but with greater emphasis on their views.

The Committee was also informed about "quick flips," which involve shareholders, directors or other senior officers of the company becoming involved in a sale of assets where they have a significant financial interest in the purchaser of the assets or in the sales transaction. The Joint Task Force noted that, in some cases, a sale of this nature may be beneficial since it may maximize realizable value for creditors. It believed, however, that such sales should only be permitted in "exceptional circumstances" unless "there was a proper sales process either subject to court supervision or conducted by persons acting independently of such persons."

The Committee also believes that there are circumstances where all stakeholders would benefit from an opportunity for an insolvent company involved in reorganization to divest itself of all or part of its assets, whether to raise capital, eliminate further loss for creditors or focus on the solvent operations of the business. We feel, however, that the Court must be involved in approving such sales and that it should be provided with some guidance

regarding minimum requirements to be met during the sale process. Finally, in our view, asset sales to shareholders, directors, officers or senior management – whether in whole or in part – should only occur in exceptional circumstances, which would include situations where it can be shown that such a sale would benefit creditors. Believing that such sales would contribute to greater fairness and efficiency, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit the debtor, subject to prior approval of the Court, to sell part or all of its assets out of the ordinary course of business, during reorganization and without complying with bulk sales legislation. Similarly, the debtor should be permitted to sell all or substantially all of its assets on a going concern basis. On an application for permission to sell, the Court should take into consideration whether the sales process was conducted in a fair and reasonable manner, and whether major creditors were given reasonable notice, in the circumstances, of the proposed sale and had input into the decision to sell. No such sale to controlling shareholders, directors, officers or senior management of the debtor having a significant financial interest in the purchaser or in the sales transaction should be permitted, other than in exceptional circumstances.

N. Governance

In insolvency proceedings, especially CCAA reorganizations and BIA proposals, all persons to whom power and authority have been given should act in good faith, competently and without conflict of interest.

In insolvency proceedings, especially CCAA reorganizations and BIA proposals, all persons to whom power and authority have been given should act in good faith, competently and without conflict of interest. They should also diligently and conscientiously perform any responsibilities they may have been given. In essence, good governance must prevail. To some extent, good governance is assured through the obligations placed on insolvency practitioners appointed or approved by the Court, including trustees, receivers and monitors. As well, it is enhanced when practitioners are licensed, and when all stakeholders act transparently.

The Joint Task Force on Business Insolvency Law Reform informed the Committee that "there is [a] need to give statutory recognition to the importance of proper governance of financially troubled businesses." It also noted that "[m]anaging the affairs of an insolvent debtor often involves balancing the conflicting interests of parties with claims of different value and priority in the face of considerable uncertainty about the values of the business and assets of the debtor." It believed that "there are certain situations … where the court should have the ability to alter the debtor's management, including by replacing some or all of the existing directors or by appointing a qualified party with some degree of authority to manage the debtor's operations."

Independence of insolvency practitioners was supported by the Canadian Bar Association, which recommended that "a general standard of independence of insolvency representatives be adopted."

The Committee has long had an interest in good governance, and has issued a number of reports addressing the principles of good governance, including our 1996 report *Corporate Governance* and our June 2003 report *Navigating through "The Perfect Storm": Safeguards to Restore Investor Confidence*. In the current context, we believe that all officers of the Court involved in proceedings under the BIA and/or the CCAA

… proper governance of the organization involved in the restructuring is required, and the organization's directors must positively assist in the restructuring efforts; …

should act in a manner characterized by good faith, competent execution of their duties and freedom from real or perceived conflicts of interest; disclosure of any circumstances that could be construed as a conflict of interest must occur. Behaviour consistent with such a standard will ensure the fairness, predictability and transparency we seek and will instil, in domestic and foreign stakeholders, confidence that our insolvency system has integrity. Moreover, proper governance of the organization involved in the restructuring is required, and the organization's directors must positively assist in the restructuring efforts; if they do not, they should be replaced and a proper governance structure implemented. For these reasons, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to permit the Court to replace some or all of the debtor's directors during proposals or reorganizations if the governance structure is impairing the process of developing and implementing a going concern solution. Moreover, prior to appointment, a trustee/monitor should disclose, to the Court, any business and legal relationships it has or has had with the debtor. The auditor or recent former auditor of the debtor should not be permitted to be the monitor. Furthermore, the monitor should not be permitted, in the event of a failed restructuring, to become the trustee or a receiver for a secured creditor.

O. Plan Approvals

In general, reliance upon "majority rule" as a voting mechanism can be problematic, since this rule can be abused by related parties or by parties who derive collateral benefits from the decisions of the group. In recognition of this potential problem, the BIA and the CCAA give the Court discretion to refuse to approve a restructuring plan or proposal even if it has received approval by a majority of the creditors. The Acts, however, provide very limited guidance about the manner in which the Court is to exercise that discretion.

While the BIA provides guidance on procedures to follow in order to secure approval of a restructuring plan, virtually no guidance in this regard is provided in the CCAA.

The Joint Task Force on Business Insolvency Law Reform informed the Committee that the BIA's provision regarding the vote of a creditor who is related to the debtor should be extended to the CCAA, and that minority creditors should be protected through a requirement "under both the BIA and the CCAA that … dissenting minority creditors will not be prejudiced by the reorganization plan as compared to a liquidation."

As a matter of fairness and predictability, and recognizing the potential for abuse of majority voting mechanisms, the Committee believes that the Court should continue to have discretion, under both the BIA and the CCAA, to not approve a restructuring plan even where the plan has the support of the majority of voting creditors. To assist the Court in determining whether it should exercise this discretion, we feel it would be useful to require the trustee or monitor to provide his or her opinion about whether dissenting creditors are likely to receive less under the plan than they would receive in a liquidation. We also feel that, in some cases, the prospect of successful reorganization is enhanced where the equity of the organization is reorganized.

… the Committee believes that the Court should continue to have discretion, under both the BIA and the CCAA, to not approve a restructuring plan even where the plan has the support of the majority of voting creditors.

At this time … neither Act gives the Court the authority to reorganize share capital.

At this time, however, neither Act gives the Court the authority to reorganize share capital. In our view, this inability limits effectiveness. We believe that the Court should have this ability, and should be able to exercise its authority to reorganize share capital, with or without consent of shareholders, who could veto an arrangement to the detriment of creditors. For these reasons, and to enhance fairness, predictability and effectiveness, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to require a trustee/monitor to provide, in connection with a request for Court approval of a reorganization plan, an opinion that, as a group, each of secured creditors and unsecured creditors are likely to receive no less under the plan than it would receive in a liquidation. Moreover, Section 54(3) of the *Bankruptcy and Insolvency Act* regarding related parties should be incorporated in the *Companies' Creditors Arrangement Act*. Finally, the Acts should be amended to provide the Court approving a reorganization plan with the power to approve a restructuring of the equity of the debtor, with or without shareholder approval.

P. Priorities

The BIA creates a priority scheme for the distribution of the proceeds of realization of the debtor's assets. This scheme, which implicitly recognizes that situations of insolvency – by definition – involve insufficient realizable assets to satisfy all claims, provides that – subject to the claims of secured creditors – certain other groups of creditors, such as employees, municipalities and landlords, have priority over other unsecured creditors in the distribution of the proceeds of realizations of the debtor's assets, subject to certain limitations.

… situations of insolvency – by definition – involve insufficient realizable assets to satisfy all claims …

The priority scheme in the BIA does not apply to CCAA proceedings or to receiverships. Moreover, provincial/territorial legislation has created statutory security interests and deemed trusts that give some claims priority over those of even secured creditors and, in any event, priority over the claims of unsecured creditors. The priority accorded Crown claims applies in the case of BIA proceedings but does not apply to CCAA proceedings or receiverships.

On the issue of differences in priorities, the Joint Task Force on Business Insolvency Law Reform commented that "[t]here is no justification for these discrepancies." It advocated the application of BIA priority rules in BIA and CCAA proceedings and in receiverships, suggesting that "[c]reditors' relative entitlements should not vary depending on the nature of the proceedings."

From the perspective of fairness, the Committee too believes that the same priority rules should govern the distribution of the proceeds of realization of the debtor's assets, regardless of the insolvency legislation under which proceedings are occurring. For this reason, the Committee recommends that:

The *Companies' Creditors Arrangement Act* be amended to incorporate the priority rules in the *Bankruptcy and Insolvency Act*.

Q. Insolvency of Other Vehicles

As a risk management tool, business – or income – trusts may be used as financing vehicles.

As a risk management tool, business – or income – trusts may be used as financing vehicles. In fact, it has been estimated that 86% of initial public offerings in Canada in 2002 were offerings of units in income trusts. In 2003, more than 100 income trusts, with more than $45 billion in market capitalization, were listed on the Toronto Stock Exchange.

At a simplistic level, a trust sells units to the public and invests in a business; the unitholders are the beneficiaries of the trust, and the trustees hold all or part of the equity interests in the business; most of the funds are advanced to the business in the form of a loan. The terms of the loan frequently provide that the before-interest-expense income of the business will be distributed to the trustees as interest, thereby reducing the taxable income of the business. In turn, the trustees distribute the moneys received to the unitholders, and the moneys are then taxed as income. From the perspective of the holder, holding a unit in an income trust is conceptually similar to holding a share in a corporation.

In the view of the Joint Task Force on Business Insolvency Law Reform, the BIA should be amended to clarify that trusts used as financing vehicles can be liquidated under the BIA, but they cannot be reorganized.

Mr. Bruce Leonard told the Committee that "[t]he problem with income trusts from a bankruptcy or reorganizational point of view is that their structure is such that it is not clear that they are covered or dealt with under either … the BIA or the CCAA. My suggestion … would be to have both [Acts] amended so that these vehicles, which are becoming so important commercially in Canada, … would be able to reorganize in the same fashion as ordinary corporations [should they fall into financial difficulty] … . I would use the definition of 'commercial trust' meaning a trust in which interests are acquired for consideration so that it is clear that it is a commercial transaction, not a family or a charitable transaction."

The Committee is aware that business trusts are increasingly popular and are being used to finance a wide range of business undertakings, including real estate, utilities, transportation, ice manufacturing, cheque printing, customs brokerage, seafood processing and natural resources. Clearly, they are becoming a tool in which investors have confidence, which is particularly important in times such as these when North America has witnessed a number of corporate scandals. Since these trusts are not accumulating retained earnings and are not re-investing in capital equipment, they are perhaps relatively more vulnerable to financial downturns. Trusts, however, are neither persons nor corporations, and consequently are not covered by either the BIA or the CCAA. We believe that, given their structure and importance as a financing mechanism for companies, they should be addressed within insolvency legislation.

We believe that, given their structure and importance as a financing mechanism for companies, [business trusts] should be addressed within insolvency legislation.

Although the Joint Task Force limited its recommendations to allowing trusts to be liquidated under the BIA, the Committee believes that circumstances could arise in which reorganization of a trust under either the BIA or the CCAA, rather than its liquidation, would be beneficial. For these reasons, and to recognize the contribution made by business trusts to the efficient operation of Canadian businesses, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be amended to provide for the liquidation or the reorganization of a business trust.

R. Income Tax

At present, the conversion of debt into equity can lead to debt forgiveness in certain circumstances, and the financial implications of debt forgiveness rules can effectively hinder reorganization.

In certain situations, insolvent debtors are able to convert debt into "distress preferred shares," which are accorded special treatment under the *Income Tax Act* but are relatively costly to create. In particular, revenue received by the holder in respect of such shares is given favourable tax treatment, since it is treated as dividend income rather than as interest income. This treatment provides a relatively low cost means of financing a restructuring.

At present, the conversion of debt into equity can lead to debt forgiveness in certain circumstances, and the financial implications of debt forgiveness rules can effectively hinder reorganization. Consequently, an insolvent debtor could sell assets rather than reorganize. Moreover, proposed distress preferred share holders frequently require a favourable tax ruling before accepting this treatment and the delays in obtaining such rules are inconsistent with the speed required in reorganizations.

The Joint Task Force on Business Insolvency Law Reform proposed to the Committee that "a creditor and an insolvent debtor [be allowed] to elect to treat a loan as if distress preferred shares had been issued." Such a change, it argued, is "aimed at both fairness and efficiency in complying with current tax policy … and [would] not require any change in tax policy … [or the *Income Tax Act*] requirements for qualifying for the tax benefit of distress preferred shares. Rather, the election is aimed at making use of distress preferred shares more accessible … . Instead of requiring an elaborate set of … transactions in order to convert the debt into distress preferred shares, parties could simply file a notice of election." Consequently, costs would be reduced, as would the time taken to make decisions and rulings; accessibility to this means of financing a restructuring would be enhanced.

The Joint Task Force also suggested that "tax policy should be neutral as between a choice of the debtor company restructured or a new corporation acquiring the business

assets, and thus the same tax treatment should be available in either situation." In its view, the debtor should be permitted to elect fresh start accounting for tax purposes as if it were a new taxpayer from the point in time when the restructuring plan is approved and effective.

The Committee feels that the costs of restructuring should be minimized, to the extent reasonably possible, in order to provide insolvent companies with an incentive to reorganize rather than become bankrupt, should that be in the best interest of stakeholders. We feel that allowing an election that would permit a loan to be treated as distress preferred shares would promote efficiency in the insolvency system. Moreover, in our view, fairness and efficiency would be enhanced if the debtor, on consummation of a plan of arrangement, is allowed to use fresh start accounting for tax purposes. Both of these changes would, we believe, lead to reorganization rather than bankruptcy, where preferable for stakeholders. For these reasons, the Committee recommends that:

The Committee feels that the costs of restructuring should be minimized, to the extent reasonably possible, in order to provide insolvent companies with an incentive to reorganize rather than become bankrupt, should that be in the best interest of stakeholders.

The *Income Tax Act* be amended to provide that distress preferred share treatment for tax purposes be afforded to qualifying debt, for a specified period of time, by filing a notice of election with the Canada Customs and Revenue Agency. Moreover, on the consummation of a plan of arrangement, a debtor should be able to elect to use fresh start accounting for tax purposes, with tax obligations relating to the period prior to the date of bankruptcy addressed as pre-filing claims.

S. Subordination of Equity Claims

Canadian insolvency law does not subordinate shareholder or equity damage claims.

Insolvency legislation in the United States has created the concept of "subordination of equity claims." Equity claims are those claims that are not based on the supply of goods, services or credit to a corporation, but rather are based on some wrongful or allegedly wrongful act committed by the issuer of an instrument reflecting equity in the capital of a corporation. Conceptually, this type of claim relates more to the loss of a claimant who holds shares or other equity instruments issued by a corporation, rather than the claims of traditional suppliers. In American legislation, such claims are subordinated to the claims of traditional suppliers.

Canadian insolvency law does not subordinate shareholder or equity damage claims. It is thought that this treatment has led some Canadian companies to reorganize in the United States rather than in Canada.

Mr. Kent, for example, told the Committee that "[i]f [a shareholders' rights claims by people who say that they have been lied to through the public markets] is filed in Canada, there is no facility in place to deal with it. They have no choice but to file in the U.S. where there is a vehicle to deal with these claims in a sensible, fair and reasonable way. In Canada, we have no mechanism. Thus, you end up with situations where it becomes difficult to reorganize a Canadian enterprise under Canadian law because our laws do not generally deal with shareholder claims."

He also indicated, however, that shareholder claims may be addressed within specific corporate statutes. Mr. Kent mentioned, in particular, the *Canada Business Corporations Act* and some provincial/territorial statutes, and shared his view that "[i]t becomes a lottery, depending on where the corporation is organized, whether there is a vehicle for dealing with some of these claims or there may not be. It is a hodgepodge system."

The Joint Task Force on Business Insolvency Law Reform shared with the Committee a proposal that all claims arising under or relating to an instrument that is in the form of equity are to be treated as equity claims. Consequently, "all [equity] claims against a debtor in an insolvency proceeding … including claims for payment of dividends, redemption or retraction or repurchase or shares, and damages (including securities fraud claims) are to be treated as equity claims subordinate to all other secured and unsecured claims against the debtor … ." It also proposed that these claims could be extinguished, at the discretion of the Court, in connection with the approval of a reorganization plan.

In view of recent corporate scandals in North America, the Committee believes that the issue of equity claims must be addressed in insolvency legislation. In our view, the law must recognize the facts in insolvency proceedings: since holders of equity have necessarily accepted – through their acceptance of equity rather than debt – that their claims will have a lower priority than claims for debt, they must step aside in a bankruptcy proceeding. Consequently, their claims should be afforded lower ranking than secured and unsecured creditors, and the law – in the interests of fairness and predictability – should reflect both this lower priority for holders of equity and the notion that they will not participate in a restructuring or recover anything until all other creditors have been paid in full. From this perspective, the Committee recommends that:

In view of recent corporate scandals in North America, the Committee believes that the issue of equity claims must be addressed in insolvency legislation.

The *Bankruptcy and Insolvency Act* be amended to provide that the claim of a seller or purchaser of equity securities, seeking damages or rescission in connection with the transaction, be subordinated to the claims of ordinary creditors. Moreover, these claims should not participate in the proceeds of a restructuring or bankruptcy until other creditors of the debtor have been paid in full.

T. Administrative Tribunals and Stays of Proceedings

At present, the CCAA gives provincial/territorial Superior Courts the power to stay "an action, suit, or proceeding brought against the company" when an insolvent company becomes subject to a CCAA order.

At present, the CCAA gives provincial/territorial Superior Courts the power to stay "an action, suit, or proceeding brought against the company" when an insolvent company becomes subject to a CCAA order. Consequently, some Courts have issued stay of proceedings orders with respect to administrative tribunals. Administrative tribunals are used to resolve disputes in the areas of labour relations, human rights, the environment, energy, transportation, communication, securities and justice, among others.

Although the Ontario Securities Commission presented testimony to the Committee, most of our witnesses focussed on administrative tribunals in one area only: labour relations. The CAW-Canada shared with the Committee its view that "the word 'or' … must be interpreted in the context of the words 'action' and 'suit,' which both refer to judicial proceedings. The common feature of the words 'action,' 'suit' and 'proceeding' is that they are judicial proceedings. The term 'proceeding' … was not intended to include extra judicial (that is non-court) proceedings such as grievance/arbitration matters, health and safety complaints before labour boards, or human rights complaints filed with human rights commissions. Regrettably, several courts … have issued wide ranging stay orders, covering administrative tribunals …, which have only an incidental impact on the financial or business affairs of an insolvent company."

The union argued that "[i]t is important to discern what the purpose of a stay order is: it is to preserve the status quo between creditors in the company by preventing any maneuvers for positioning among creditors during the interim stay period which would give an aggressive creditor an advantage to the prejudice of others, …, and would further undermine the financial position of the company, making it less likely that the eventual 'arrangement' would succeed. … If a broad stay order suspending the prosecution of employment rights disputes is issued in favour of an insolvent corporation

… then the CCAA has been used to place the insolvent company in a better position than it was before the statute was triggered. … [T]he statute is designed to preserve the status quo, not put the insolvent corporation in a better position, and fundamentally above the law."

In the view of the CAW-Canada, the CCAA should be clarified in order to exempt, from the application of a stay of proceedings, all employment-related proceedings brought before non-judicial administrative tribunals. It told the Committee that "a working grievance and arbitration process is critical if day to day issues in the workplace are to be resolved with a minimum of disruption. … Grievances routinely deal with both monetary and non-monetary matters, including, for example, health and safety issues, sexual harassment complaints, discrimination complaints, and providing remedies for employees who have been wrongfully disciplined, or whose employment [has] been wrongfully terminated. … [T]he remedies afforded by the grievance and arbitration process are not in the nature of a pre-filing debt or liability which can be compromised under the CCAA." It believed that there is no justification for eliminating recourse to the grievance arbitration process while employees continue to work for a company undergoing reorganization.

In the Committee's view, administrative tribunals decide a number of issues that are important to Canadians. While employees themselves are probably the main beneficiaries of decisions in certain labour relations matters, society benefits – in a broad sense – from the existence of human rights tribunals to safeguard the protection from discrimination that our nation desires. Moreover, administrative tribunals decide issues in a number of other areas that have a public interest component, including disputes related to the environment, justice and securities, among others. We generally believe that a stay of proceedings granted under the CCAA should not apply to the activities of administrative tribunals, since many of their decisions are made in areas that clearly fall within the public interest.

We believe that a stay of proceedings granted under the CCAA should not apply to the activities of administrative tribunals, since many of their decisions are made in areas that clearly fall within the public interest.

The Court and commentators have justified staying proceedings of administrative tribunals by asserting that the

… an appropriate balance must be sought between the fundamental importance of a broad range of administrative proceedings in our current environment and the need to focus the attention of directors and senior management on a successful reorganization.

energy and attention of the directors and senior management of companies undergoing reorganization should be devoted – virtually entirely – to the reorganization, and not diverted or distracted by the requirement to deal with administrative proceedings. As is the case in some other areas, however, an appropriate balance must be sought between the fundamental importance of a broad range of administrative proceedings in our current environment and the need to focus the attention of directors and senior management on a successful reorganization.

While allowing administrative tribunal activities to continue would support the fundamental principles of fairness and predictability that we are seeking in our insolvency system, we feel that directors and senior management of corporations in reorganization procedures must remain focused on the goal of a successful reorganization. Consequently, the Committee recommends that:

The *Companies' Creditors Arrangement Act* be amended to exempt, from the application of stays of proceedings and subject to Court discretion, all proceedings brought before non-judicial administrative tribunals. The exemption should be granted where two conditions are met: the exemption is needed for the protection of third parties; and the exemption does not subject directors or senior management to undue pressure and loss of time.

CHAPTER SIX:
THE SENATE COMMITTEE'S EVIDENCE AND RECOMMENDATIONS ON ADMINISTRATIVE AND PROCEDURAL ISSUES

A. Volume of Filings, Access to the Process and Funding of the Office of the Superintendent of Bankruptcy

The *Bankruptcy and Insolvency Act* gives the Office of the Superintendent of Bankruptcy (OSB) several responsibilities. The Office: supervises the administration of bankruptcy estates, business reorganizations, consumer proposals and receiverships under the Act; keeps records of insolvency proceedings that occur under the Act; records and investigates complaints by creditors, debtors and the general public; and licenses and oversees the trustees who administer bankruptcy estates under the Act.

Since becoming a Special Operating Agency in 1997, the OSB has depended exclusively on income generated by its operations to fulfill its statutory mandate. Adopting a user-pay principle, a variety of fees exist: filing fees; levies on dividends payable to creditors; licence fees; and fees for searching the public record. Although the OSB does not use the funds, the Superintendent administers an account for unclaimed dividends and undistributed funds. In August 2003, there was about $9.3 million in the fund.

Although the OSB does not use the funds, the Superintendent administers an account for unclaimed dividends and undistributed funds.

The OSB's responsibilities and powers were increased by the 1992 and 1997 amendments to the BIA. These responsibilities, together with the increase in commercial and consumer bankruptcies over time and the increased complexity of cases, have generated comments on the need for more resources for the OSB.

A focus on prevention raises the question of how programs and initiatives should be funded.

Moreover, there has been speculation about the role that enhanced education and preventive approaches to insolvency might play in reducing financial difficulties, and thereby insolvency, among individuals and businesses. To be effective, education and prevention measures must be offered at the correct time and in the correct manner. A focus on prevention raises the question of how programs and initiatives should be funded. In addition, it is important to encourage studies and research, predominantly but not exclusively, by academics. In the past, the OSB has benefited significantly from such research, but there are insufficient funds to research broader subjects, such as credit granting practices in Canada and other issues that would help Parliament to determine the direction and scope of future amendments to Canadian insolvency legislation.

The OSB plays no supervisory or administrative role with respect to the *Companies' Creditors Arrangement Act*; any records that exist about the growing number of proceedings under the Act are resident with the Court in which the cases were commenced. It is perhaps for this reason that limited data exists about activities under the Act. Consequently, it is virtually impossible to assess meaningfully the effectiveness of proceedings under the CCAA, the frequency with which companies initiate procedures under the Act, the characteristics of these companies, and the consequences of the Act and its operations for Canadian companies and the Canadian economy.

The inability to carry out an assessment of the operations and effectiveness of proceedings under the CCAA might have particularly serious consequences, since many of Canada's large businesses that experience financial difficulties pursue options under the CCAA. Moreover, the absence of supervisory oversight and lack of data may undermine the trust of lenders and investors, with potentially negative implications for the economy.

Witnesses commented on a wide range of issues, including the current role of the OSB and how it should be

expanded, access to the process supervised by the OSB, funding concerns related to the Office, the lack of CCAA-related data and other information because of the absence of supervisory oversight, and the importance of research and preventive measures.

A number of witnesses shared with the Committee their views on how the role of the Office of the Superintendent of Bankruptcy should be expanded. The Union des consommateurs, for example, recommended that the Office establish a procedure that would require trustees to "standardize the information to be given … to debtors" and that it organize or contribute to "outreach campaigns on credit, debt overload and their consequences." The group also identified the need for a practical "how to" manual for debtors – containing information on their responsibilities and those of the trustee, as well as on procedural issues – written in a manner that is easily understood by users, without excessive use of specialized terminology.

Others, including a number of professors of law represented by Professors Ziegel and Telfer, identified the need for research to enable policy makers and stakeholders to make informed decisions about how the existing system works and the likely impact of various policy options; they envisioned the Office playing a role regarding research. In particular, they recommended: the establishment of an annual budget for insolvency research purposes; the establishment of an advisory committee to advise Industry Canada and the Office of the Superintendent of Bankruptcy on research projects to be initiated during the year; public announcements about these initiatives to promote visibility and transparency; and greater collection of insolvency data, especially about consumer insolvencies and reorganizations under the CCAA.

… the need for research to enable policy makers and stakeholders to make informed decisions about how the existing system works and the likely impact of various policy options …

Professors Ziegel and Telfer also advocated an expanded role for the OSB when they recommended that it have record keeping and administrative functions with respect to the CCAA. To help finance expenses associated with these functions, they believed that CCAA estates should be required to contribute a "modest" levy. Moreover, they felt that the

Superintendent of Bankruptcy should have a role in "CCAA hearings where important constituencies are not represented or major issues of public policy or interpretation of the legislation are at issue." As examples of the latter, Professors Ziegel and Telfer mentioned: whether a CCAA Court has the power to oblige the debtor and its unions to reopen collective agreements, whether the Court can excuse a debtor from remitting collections held in trust for another party, and whether an order can be made binding third parties who are not involved in the CCAA proceedings.

Commenting on access to the bankruptcy process, Professors Ziegel and Telfer informed the Committee about the Federal Insolvency Trustee Agency (FITA), through which the federal government made low-cost bankruptcy services available via regional offices of the OSB. Although this Agency no longer exists, they believed that it was useful in enhancing access for low-income debtors.

A different view on supervision was presented to the Committee by the Canadian Bankers Association, which did not support the implementation of a supervisory regime for the CCAA without additional study. Regarding funding of the OSB, the Association told us that it would object to any increase in user fees as a means of increasing funding for the OSB's operations. It believed that "[i]ncreased costs reduce the ability of creditors to recover their funds."

In support of greater use of technology, the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada shared their view that "[f]urther opportunities need to be explored for electronic communications. Transparency and accessibility could be enhanced further by the use of electronic access to information."

The Committee believes that the Office of the Superintendent of Bankruptcy plays a key supervisory and administrative role with respect to the BIA, and provides high quality services to stakeholders despite budgetary pressures.

The Committee believes that the Office of the Superintendent of Bankruptcy plays a key supervisory and administrative role with respect to the BIA, and provides high quality services to stakeholders despite budgetary pressures. Its existence, and the actions it takes in such areas as ensuring

compliance with the legislation and safeguarding transparency, accountability and integrity, help to ensure that all Canadians, Canadian companies and foreign investors benefit from an insolvency system that is characterized by the highest level of integrity. We applaud the Superintendent and others in the Office of the Superintendent of Bankruptcy and encourage them to continue with their efforts to ensure that Canada continues to be regarded as having an insolvency system that ranks among the best in the world.

The Committee has heard the concerns about inadequate funding for the OSB and the notion that Canadian taxpayers should contribute to the funding of operations because of the benefits that the country enjoys as a consequence of the Office's compliance and supervisory efforts. Nevertheless, we support a strict application of the user-pay principle, and believe that fees must be set at a level sufficient to enable the Office to carry out its statutory duties responsibly.

The Committee believes that the greater use of technology and a streamlining of the bankruptcy process for consumers and companies will help to constrain fee increases, since further fee increases may negatively affect access to the insolvency process. In our view, the adoption of new technology must be a priority in our economy whenever it has the potential to improve efficiency, effectiveness, accessibility and equity. From this perspective, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be reviewed in order to identify opportunities that will contribute to greater efficiency within the insolvency system, including efforts regarding the adoption of new technologies.

Industry Canada's *Report on the Operation and Administration of the* Bankruptcy and Insolvency Act *and the* Companies' Creditors Arrangement Act presents the question: should the concept of universal access to bankruptcy services be redefined, with new measures to ensure access, or should

… the Committee believes that access to the bankruptcy system is increasingly compromised for low-asset, low-income debtors, although the OSB's Bankruptcy Assistance Program is useful in providing access to some debtors.

access cease to be seen as a right? Like our witnesses, the Committee believes that access to the bankruptcy system is increasingly compromised for low-asset, low-income debtors, although the OSB's Bankruptcy Assistance Program is useful in providing access to some debtors. We believe that this Program is important to help ensure the access that is a fundamental principle underlying the insolvency system we seek, and applaud those trustees who provide their time and expertise without payment.

The Committee, like a number of our witnesses, is of the opinion that research, education and prevention are critically important. We are particularly concerned about the lack of data related to the CCAA, about the lack of a research program that would help to identify the causes of bankruptcy and thus assist in the development of appropriate solutions, and about the extent to which prevention of insolvency may begin with the proper type of education delivered at the proper time.

Clearly, the current resources of the OSB do not permit it to fund initiatives in these areas, and the Committee firmly believes that fees must not be increased in order to finance this type of research, education and prevention. Instead, we believe that the account administered by the Superintendent which contains unclaimed dividends and undistributed funds should be reallocated to these uses, particularly to a research program to be directed and overseen by the OSB. At the end of August 2003, that account contained more than $9.3 million, as noted above. In our view, dividends that remain unclaimed and funds that remain undistributed after a two-year period should be allocated to research and education. In stipulating a two-year period, the Committee intends that sufficient funds should always be retained to pay claims, and does not intend that claimants should be barred from claims after two years. Under no circumstances, however, should these funds be used to finance the operations of the OSB. Research and education would hopefully assist in ensuring efficiency, effectiveness and responsibility. It is for these reasons that the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to provide the Superintendent of Bankruptcy with the authority to finance research and education programs from the account which contains unclaimed dividends and undistributed funds. Amounts that are unclaimed or undistributed after a two-year period should be used in this way.

B. Consolidation of Insolvency Statutes

The phrase "historical circumstances" has been used to describe why Canada has two insolvency statutes under which companies can reorganize. In 1923, reorganizations under the BIA were restricted to debtors who were actually bankrupt. The CCAA was introduced in the 1930s to assist companies that were insolvent but not bankrupt, although companies rarely used it for the next five decades.

Although amendments were made to the CCAA in 1997 to align more closely its provisions with those of the BIA, debate continues about whether these reorganization statutes should be combined, whether the status quo should prevail, or whether the CCAA should be repealed. As noted in Chapter Three, the BIA is viewed as providing a relatively predictable and consistent outcome, particularly when compared to the CCAA. The CCAA is thought, however, to give the flexibility needed in certain situations, which might be the case with larger businesses that are attempting to restructure. The financially troubled company selects the statute under which it wants to reorganize, subject to the threshold requirements of the CCAA.

Under the CCAA, the Court appoints a monitor to oversee the reorganization, and he or she files reports with the Court on the state of the insolvent company's finances. This process is analogous to what occurs with a reorganization under the BIA, where a trustee files reports with the Office of the Superintendent of Bankruptcy. The statutes do differ, however, since the Court makes or approves most decisions under the CCAA while, generally, under the BIA the Court is involved only in sanctioning a proposal that has already been approved by creditors.

Because of the relative flexibility and lack of predictability associated with the CCAA process, some creditors perceive that they are disadvantaged relative to the

outcome that would occur under the BIA. In the absence of data regarding proceedings under the CCAA, this perception can be neither affirmed nor disputed. One means of ensuring data on this issue, as well as others related to the CCAA, might be providing the Office of the Superintendent of Bankruptcy with a supervisory and administrative role with respect to both the CCAA and the BIA, as has been suggested by some. Another option, however, involves the research program recommended earlier in this Chapter. Either option does not, however, exclude the other.

Witnesses presented a range of views to the Committee on the issue of whether the BIA and the CCAA should be merged or retained as separate statutes. The Canadian Bankers Association told us that the current system of separate statutes recognizes the needs of both smaller and larger organizations. Similarly, the Joint Task Force on Business Insolvency Law Reform supported the status quo, with the CCAA for the reorganization of large companies, and the BIA for smaller corporations and other entities. It shared with us the view that "Canada's experience with two reorganization systems has generally been positive. The principal virtue of the two-system approach is that it responds to the fact that different types of reorganization legislation are appropriate for different types of debtors." The Joint Task Force, however, also noted that retention of separate statutes "should not preclude harmonization of specific provisions of the CCAA and the BIA" and made particular mention of reviewable transactions and filing requirements.

Witnesses presented a range of views to the Committee on the issue of whether the BIA and the CCAA should be merged or retained as separate statutes.

Professor Keith Yamauchi, of the Faculty of Law at the University of Calgary, supported the status quo as well, and argued that "[t]he flexible, court-driven nature of a proceeding under the *Companies' Creditors Arrangement Act* lends itself to large multinational entities." At the same time, "the rigid provisions of the *Bankruptcy and Insolvency Act* fit quite nicely with the reorganization of small to medium-sized businesses." He believed that the system in Canada "works well from a practitioner's perspective." The wide judicial discretion given by the CCAA's provisions has not been abused, in his view, but has instead been used "wisely to

effect results that could not otherwise be reached in a strict, rule-oriented system."

Professor Janis Sarra, of the Faculty of Law at the University of British Columbia, also noted the benefits of the flexibility inherent in the CCAA, and informed the Committee that "the courts and parties affected by … corporate insolvency have been able to utilize the relatively flexible process under the CCAA in order to arrive at successful restructurings that are reflective of the appropriate balance of various interests in such proceedings." In speaking to us, she underscored the importance of the interests of workers, communities and the broader public interest.

The Committee believes that, fundamentally, the current system is working well, which does not mean that changes are not required for the benefit of all domestic and international stakeholders. For example, changes may be required to ensure the collection of data about proceedings under the CCAA, and some matters that are not addressed in the CCAA – but are covered in the BIA – should be considered. Stakeholders have now gained experience with the process under both statutes and jurisprudence has developed. We believe that the CCAA should continue to exist for companies with a relatively high level of indebtedness, while the BIA should be available for all organizations; the level of indebtedness required to take action under the CCAA should, however, be reviewed on an ongoing basis to ensure its continued relevance. There were historic reasons for two separate statutes, and these reasons continue to have importance today. The CCAA appears to be relatively effective in assisting larger companies in their reorganization efforts, while the BIA seems to be working well for smaller organizations.

The CCAA appears to be relatively effective in assisting larger companies in their reorganization efforts, while the BIA seems to be working well for smaller organizations.

In deciding whether to recommend the status quo or an integration of the statutes, the Committee was mindful of the fundamental principles outlined in Chapter Two. In particular, we know that the flexibility that is inherent in the CCAA is probably inconsistent with consistency and predictability, and may not result in fairness. Nevertheless, tradeoffs must be

made and an appropriate balance must be struck. We believe that the need for flexibility is paramount with the CCAA, but urge relevant parties to respect the principles of predictability, consistency and fairness – to the extent that they can – when involved in proceedings under the Act. For this reason, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* continue to exist as separate statutes.

C. Statutory Review of Insolvency Legislation

The BIA and the CCAA require that a Parliamentary review of their administration and operation occur five years after the coming into force of the relevant sections, which occurred in 1997. Although late by one year, the current examination by the Standing Senate Committee on Banking, Trade and Commerce fulfills this requirement for statutory Parliamentary review.

Witnesses told the Committee that ongoing review of insolvency legislation in Canada is needed. While the current review of the BIA and the CCAA by this Committee was welcome, in their view it must occur regularly in order to ensure that Canada's insolvency legislation: meets the needs of all stakeholders in the best possible manner; continues to accommodate the changing socio-economic conditions of an evolving society and the challenges that this change implies for stakeholders; and remains consistent with – although not identical to – the insolvency regimes that exist worldwide but most particularly those of our major trading partners. Mr.David Baird, Q.C., of Torys LLP, told us that "the reform process never ends and further reforms of our bankruptcy and insolvency legislation are required to keep that legislation effective and efficient." Furthermore, the Joint Task Force on Business Insolvency Law Reform indicated that "because of the remarkable pace of change in insolvency law and practice, it is advantageous to continue with regular five-year reviews of insolvency statutes for continuous improvements, as well as to reflect changed circumstances and new developments."

While the Committee's review was limited to the BIA and the CCAA, witnesses also commented on the need for ongoing statutory Parliamentary review of two additional insolvency statutes – the Winding-up and Restructuring Act *and the* Farm Debt Mediation Act.

While the Committee's review was limited to the BIA and the CCAA, witnesses also commented on the need for ongoing statutory Parliamentary review of two additional insolvency statutes – the *Winding-up and Restructuring Act* (WURA) and the *Farm Debt Mediation Act* (FDMA). Regarding the former Act, Mr. Baird shared his view that revisions are needed that would "make the restructuring of financial institutions much more efficient and cost effective. This would greatly enhance the recovery for consumers and other creditors of insolvent financial institutions." Describing

the WURA as "an insolvency statute that has been very neglected and has not received a comprehensive review for more than 100 years," he made particular mention of the recommendations made by the Insolvency Institute of Canada for amendments to the WURA and told us that the Act should contain a comprehensive scheme for the restructuring of a financial institution. In its presentation to us, the Canadian Bankers Association supported a limitation on the WURA's application to financial institutions in order to "eliminate overlap, increase efficiency and facilitate efforts to tailor the WURA to the needs of financial institutions."

The *Farm Debt Mediation Act* requires the Minister of Agriculture and Agri-Food to undertake a review of its operations every three years, and to table a report in Parliament. The Act, however, stipulates only that the Minister may, for this purpose, consult with representatives of appropriate organizations. Mr. Brian O'Leary, Q.C., of Burnet, Duckworth & Palmer LLP, told the Committee that it "would be prudent to have the [*Farm Debt Mediation Act*] reviewed every 5 years along with the BIA and the CCAA."

Regarding the WURA, the Committee feels that while its application is limited to financial institutions, it too is an important pillar in our insolvency system that should receive ongoing review by Parliament, particularly since there has been – and is likely to continue to be – merger and acquisition activity in this sector and our financial institutions are critically important to the health and prosperity of an economy such as ours. The FDMA, too, is an important insolvency statute for a particular part of our economy. Canada's agricultural industry faces ongoing challenges, and these challenges sometimes result in unsustainable levels of debt for Canadian farmers. The FDMA must also be reviewed by Parliament on a regular basis to ensure that it is continuing to meet the needs of stakeholders in the agricultural industry in the best possible manner.

The Committee strongly believes that statutory Parliamentary review of the operation and administration of

We fear that if our insolvency regime – as part of the set of laws designed to contribute to the health and prosperity of Canadians and the Canadian economy – differs markedly from – or is less effective than – that in other countries, negative economic consequences would be the result.

federal legislation is useful in a range of areas, including insolvency. Given our particular focus at this time, however, and testimony from our witnesses about the need to ensure that Canada's insolvency regime continues to meet the evolving needs of domestic and international stakeholders and recognizes the changing socio-economic environment, we are firmly convinced that ongoing Parliamentary review of our four insolvency statutes must occur. One way to ensure that needed review occurs is statutory provisions to that effect. We fear that if our insolvency regime – as part of the set of laws designed to contribute to the health and prosperity of Canadians and the Canadian economy – differs markedly from – or is less effective than – that in other countries, negative economic consequences would be the result. Our insolvency system must be at least as efficient, effective and fair as those found in other countries. From this perspective, and to ensure the efficiency and effectiveness that we seek, the Committee recommends that:

The *Bankruptcy and Insolvency Act*, the *Companies' Creditors Arrangement Act*, the *Winding-Up and Restructuring Act* and the *Farm Debt Mediation Act* be amended to require a review by a Parliamentary committee at least once every five years.

Although not, strictly speaking, an issue related to statutory Parliamentary review, the Committee would like to comment on the recommendation made by Professors Ziegel and Telfer that "an advisory committee of outside experts [be appointed], similar in purpose to the Colter Committee of 1984, to prepare draft provisions for the federal government's consideration." Throughout our study, we have assumed that legislation to amend Canada's insolvency laws would result from our review, and in a timely manner. There is, however, no guarantee that legislation will be introduced in Parliament expeditiously or that, if it is, it will become law. Certainly, when one considers the number of insolvency-related legislative attempts that have died on the Order Paper, there is perhaps cause for pessimism rather than optimism. It was perhaps from this perspective that Professors Ziegel and Telfer

made their recommendation to allow outside experts to draft the legislation in order to assist in a timely amendment process.

The socio-economic environment has changed since the last substantive amendments to the BIA and the CCAA in 1997. The Committee believes that all laws in Canada, but particularly those of fundamental importance to the health of our economy and our citizens, must be reviewed and amended regularly to ensure that they meet their intended goals in the best possible manner. From this perspective, we urge the federal government to introduce amendments to the BIA and the CCAA – and perhaps to the WURA and the FDMA as well – at the earliest opportunity, and certainly no later than the first session of the next Parliament.

D. A Specialized Judiciary

Certain areas of the law implicitly recognize the benefits of specialized knowledge.

Certain areas of the law implicitly recognize the benefits of specialized knowledge. For example, the privative clauses that exist to protect decisions made by administrative tribunals – including labour relations and human rights, among others – recognize the specialized perspective and background that tribunal members bring to the fulfillment of their duties and to the decisions they make. In these cases, appeals to the Court are limited in part because the Court generally lacks specialized expertise in those particular areas.

Witnesses supported the development of a specialized judiciary to hear and resolve insolvency cases within Canada. The International Insolvency Institute, for example, told the Committee that "a greater degree of specialization in administering bankruptcies and reorganizations would be beneficial both in enhancing the interests of stakeholders in reorganizations and in furthering the Canadian public interest in having an experienced, understandable and predictable system for reorganizations and restructurings." In the Institute's view, however, a specialized insolvency judiciary probably could not be achieved under the existing system, where provincial Chief Justices designate the judges to deal with insolvency matters. Consequently, it suggested that responsibility for designating these judges be given to the Governor in Council on the recommendation of the Chief Justice.

The Committee was also informed that, to some extent, this specialization is already beginning to develop and some uniformity in decision making exists across Canada. Professor Yamauchi indicated that "provincial judicial bodies … are, for lack of a better term, starting to create specialist judges to deal with reorganizations. … In terms of getting uniformity across the country, it seems … that most of the judges refer to cases from other jurisdictions and do their balancing to come out with a fair and reasonable approach for all of the stakeholders." Mr. Mendelsohn, of Mendelsohn, G.P, also

commented on the issue of specialization, arguing for the creation of "more specialized judiciaries in the major centres of Canada."

This Committee has long been a supporter of specialization, training and education. For example, in our June 2003 report *Navigating Through "the Perfect Storm": Safeguards to Restore Investor Confidence,* we recommended the development of specifically tailored education and training initiatives to enhance the knowledge of board directors. We, like a number of our witnesses, believe that judges with specialized knowledge of insolvency matters are best equipped to resolve cases in the best interests of all stakeholders. We do not, however, believe that specialization should be limited to insolvency; more generally, we support the development of specialized judges in the full range of areas that are decided by our Courts. We are pleased that some specialization already seems to exist with respect to insolvency and that judges appear to be deciding cases in a relatively uniform manner across the country. Nevertheless, we support formal specialization through education and training programs, and believe that these programs will assist in the uniformity, consistency and predictability that we feel are important.

We … believe that judges with specialized knowledge of insolvency matters are best equipped to resolve cases in the best interests of all stakeholders.

A question then arises about how this specialized knowledge is acquired. While it might occur simply through hearing repeated insolvency cases – through "on-the-job training," if you will – the Committee believes that more must be done. In the same manner that courses are being developed and offered to individuals to make them more knowledgeable members of boards of directors, we feel that education and training programs must be developed that would enable judges – who may currently adjudicate the full range of cases before the Court – to develop specialized expertise in the area of insolvency. We wonder whether the National Judicial Institute might play a useful role in this regard. Feeling that a specialized insolvency judiciary would contribute to the fairness, predictability and consistency that we believe are important in our insolvency system, the Committee recommends that:

The federal government consult with relevant stakeholders with a view to developing education and training programs that would enable judges in Canada to develop specialized expertise in the area of insolvency law.

E. Issues of Costs

The insolvency process, insofar as the payment of professional fees is concerned, is internally financed, with fees paid to trustees, monitors and lawyers, among others. Trustees are paid from the funds generated by the estate, in priority to the claims of other creditors, and the level of trustees' fees may either be determined by the creditors or, where this is not the case, paid pursuant to a tariff based on a percentage of the total value of realized unsecured assets – presently 7.5% – subject to variation by the Court through the process known as "taxation," that is, approval of fees.

Similarly, the monitor appointed during restructuring under the CCAA receives fees for services rendered, as approved by the Court, throughout Canada, with the exception of Quebec where the fees are determined – in the first instance – by agreement between the monitor and the debtor. While the CCAA does not specify the priority given to the payment of monitors' fees, in practice the debtor pays the fees to the monitor as an administrative cost during the restructuring process and ranking ahead of the creditors.

In CCAA proceedings, the debtor will usually – although not always – pay the legal costs of creditor groups, which generally enhances their cooperation during the restructuring process.

When litigation arises, the losing party is generally required to pay legal costs – sometimes referred to as judicial costs – to the lawyer of the winning party. This practice is intended to defray, in some measure, the cost of litigation that the winning party has incurred. These judicial costs are payable according to the Tariff of Costs contained in the Act.

Mr. Baird shared his views with the Committee regarding the Tariff of Costs. After noting that the tariff was introduced five decades ago and has not been revised since

that time, he suggested that it is "completely outdated" and that "[i]n most jurisdictions, the tariff has been ignored." He believed that the Tariff of Costs should be repealed and the BIA amended to provide that, should the losing party be obliged to pay the legal costs of the winning party, the Tariff of Costs applicable in the province/territory in which the litigation occurs should apply.

Representatives of organized labour suggested to the Committee that trade unions should have their costs paid, and the Canadian Labour Congress told us that "[union] costs related to a restructuring are not always paid in the same way as the costs of other creditor groups." The labour federation suggested that "[i]f a company or an estate has sufficient funds to pay a trustee in bankruptcy or a monitor and their legal counsel respectively, then a company or estate should also be made to pay the legal costs incurred by a trade union (or by unorganized employees) to advance their claims in the insolvency proceedings. … Further, the payment of the legal costs of trade unions and employees would facilitate their organization (in a multi-union environment) into one cohesive group which can be dealt with by the estate in a much more streamlined manner … ."

A tariff that allows a cost of $1.00 for a letter or $4.00 to $6.00 for the drafting of assignments, proposals or statements of claim bears no relationship to the realities of today.

The Committee is aware of the Tariff of Costs which, since it has not been amended since 1949, has no practical relevance today. A tariff that allows a cost of $1.00 for a letter or $4.00 to $6.00 for the drafting of assignments, proposals or statements of claim bears no relationship to the realities of today. We know that various *ad hoc* practices have been developed to overcome this problem, and that while the BIA permits recourse to the regular Tariff of the Court, this civil tariff cannot – in the absence of legislation – displace the Bankruptcy Tariff in its entirety. Moreover, the CCAA makes no provision for a tariff; consequently, costs that are incurred under the CCAA follow the tariff of ordinary civil cases.

In contemplating how to address the problems associated with the Tariff of Costs, the Committee decided that the best course of action is to abolish it and instead use the civil Court tariffs as they apply across the provinces/territories.

We do not support updating the Tariff that currently exists, since there is a danger in leaving a Tariff schedule in legislation that may be updated only infrequently. Nor do we believe that providing the Governor in Council with the regulatory authority to set tariffs is appropriate, since there is an easier and more logical solution available: use civil Court tariffs.

… there is an easier and more logical solution available: use civil Court tariffs.

These tariffs are the preferred solution for the Committee because they already exist, and because they presumably reflect regional variations and the judgments of various provincial/territorial legislatures as to the extent that judicial costs should or should not fully or substantially compensate – or indemnify – the winning party at the expense of the losing party. Some provinces/territories provide for substantial or full indemnification, while others provide only for relatively modest tariffs of costs in order to avoid discouraging those with relatively modest means from pursuing their rights before the Court. We believe that using the Tariff of Costs applicable in the province/territory in which the litigation occurs would respect a number of the fundamental principles identified by us as important, including fairness and predictability; it would also provide an element of transparency. Consequently, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to repeal the Tariff of Costs. Instead, costs should be paid in accordance with civil Court tariffs as they apply from place to place throughout Canada.

F. Conflicts of Interest

Debtors who file for bankruptcy under the *Bankruptcy and Insolvency Act* give control of their assets to a trustee, who has a variety of roles: to advise the debtor who is paying his or her fees; to maximize the returns to creditors from the sale of non-exempt assets in the bankrupt's estate and to distribute them in accordance with the provisions of the Act; and, more generally, to carry out his or her duties with respect to administering the bankruptcy while maintaining the integrity of the BIA. These multiple roles may create conflicts of interest for the trustee.

Professors Ziegel and Telfer noted the potential for conflicts of interest, and told the Committee that "once bankruptcy has ensued or the debtor has made a consumer proposal the trustee owes duties to the debtor's creditors and to the court. This gives rise to a conflict of interest between the trustee's duty to the consumer and his [or her] duties to the creditors and the court." In their view, adoption of some of the recommendations made by the Personal Insolvency Task Force would add to this conflict.

The [CCAA] is silent with respect to qualification requirements and rules of professional conduct and, like trustees, monitors may face conflicts of interest.

The CCAA requires the appointment of a monitor to oversee the affairs and finances of the insolvent company during the reorganization period, in accordance with the orders of the Court. The Act is silent with respect to qualification requirements and rules of professional conduct and, like trustees, monitors may face conflicts of interest.

In speaking to the Committee about the role played by monitors in CCAA proceedings, Equifax Canada Inc. voiced the view that "most other systems … provide more transparency and are much freer from conflicts of interest … . Canada should be able to devise a standard of independence that would ensure that insolvency officeholders are free from other interests and other relationships that might impact on their objectivity and their ability to serve creditors they are appointed to represent."

The organization went on to note that "[m]onitors are expected to act in a variety of inconsistent and conflicting roles. It is commonplace for monitors to act as a financial consultant to the debtor, as a financial consultant to the secured creditors of the debtor, as a trustee in bankruptcy representing the interests of unsecured creditors, or as a receiver or receiver and manager representing the interests of secured creditors. It is not unusual for a monitor to occupy one or more of these roles in sequence as a case develops and there are examples of monitors occupying all of these positions *at the same time*." As a solution, Equifax Canada Inc. advocated improved guidelines in the BIA and the CCAA regarding conflicts of interest and the duties of officeholders.

The Committee is firmly of the opinion that roles and responsibilities that would create conflicts of interest – whether real or perceived – for trustees, monitors or other insolvency practitioners must be avoided.

The Committee is firmly of the opinion that roles and responsibilities that would create conflicts of interest – whether real or perceived – for trustees, monitors or other insolvency practitioners must be avoided. If other stakeholders perceive these individuals to be in a position of conflict, then their faith in the integrity of our insolvency system and their sense of fairness in the process are reduced. While this occurrence has negative implications for Canadian stakeholders, the effects extend to foreign investors and thereby to the Canadian economy. The insolvency system in Canada must be – and must be seen to be – fair and transparent. Consistent with the desire to uphold these fundamental principles, the Committee recommends that:

The *Bankruptcy and Insolvency Act* and the *Companies' Creditors Arrangement Act* be reviewed in order to identify and eliminate any opportunities for the roles and responsibilities of insolvency practitioners to place them in a real or perceived conflict of interest. Moreover, in order to ensure that all practitioners fulfill their duties with a high level of integrity, the federal government should adopt guidelines for insolvency practitioners regarding professional conduct and conflicts of interest, expanding upon Rules 34 to 53 of the *Bankruptcy and Insolvency Act* where appropriate.

G. The Definition of Income

Under the BIA, not all of a bankrupt's financial resources are treated equally. The Act specifies that non-exempt assets are available to the trustee for liquidation and hence for administrative costs and distribution among creditors.

"Assets" and "income" are treated differently under the [BIA].

"Assets" and "income" are treated differently under the Act. All assets of the bankrupt, other than exempt assets, are vested in the trustee upon the bankruptcy of the debtor. Income earned by the debtor during his or her bankruptcy and prior to discharge remains with the debtor in order to permit him or her to maintain a reasonable standard of living for himself or herself and his or her family. Where the income of the debtor exceeds certain standards, however, the income – referred to as excess or surplus income – is to be paid to the trustee for distribution to creditors after payment of administrative expenses. This situation is perceived to be a fair treatment of the debtor's income during bankruptcy, since income that exceeds the debtor's needs should properly be used to reimburse the creditors to the extent possible.

Prior to amendments to the BIA in 1997, income was defined as "salary, wages or other remuneration from a person employing the bankrupt." Changes in 1997 subjected "income" to a needs test involving "all revenues of a bankrupt of whatever nature or source." While the usual interpretation has been income both earned and received during bankruptcy – with any income earned before the date of filing for bankruptcy and received after the date vesting with the trustee absolutely and not included in the needs analysis – recent Supreme Court of Canada decisions have resulted in the application of the needs analysis to income entitlements arising from pre-bankruptcy events, such as personal injury awards, pay equity settlements and wrongful dismissal damages. The result has been that these types of non-periodic, lump-sum,

pre-bankruptcy entitlements received after bankruptcy have been classified as income.

In the view of the Personal Insolvency Task Force, "income" has three characteristics: it is earned through labour market activity; it is generally intended to finance the costs of current consumption; and it is generally received on a periodic basis. Wages and salaries are income, while lottery winnings and inheritances are not.

The Task Force recommended that the BIA be amended to clarify the definition of "income." In particular, it believed that the term "total income" should be defined to include revenues earned at any time before the date of discharge, including revenue earned before the date of bankruptcy, that have not been received before the date of bankruptcy. To the extent that pre-bankruptcy income entitlements received after the date of bankruptcy are not required to meet the current financial needs of bankrupts and their families, the entitlements should accrue in full to the trustee for distribution to creditors; if these financial needs are being met out of current income, creditors could realize higher levels of recovery.

Moreover, the Task Force believed that guidance should be given to trustees about the manner in which lump-sum entitlements should be allocated between bankrupts and creditors; guidance in this area should result in consistency and predictability. Finally, trustees should acquire, for distribution among creditors, any tax refund to which the bankrupt is entitled in his or her pre-bankruptcy return and post-bankruptcy return, as well as any tax refund for any prior year.

The Task Force's recommendations were supported by a number of the Committee's other witnesses. For example, the need for clarification of the term "total income" was also highlighted by Professors Ziegel and Telfer, and the Task Force's position was supported by the Canadian Bar Association, which told the Committee that "[r]ecent case law has rendered reform necessary." The Canadian Association of

Insolvency and Restructuring Professionals and the Insolvency Institute of Canada too expressed support for the Task Force's recommendations.

The view of the Canadian Bankers Association went somewhat farther than the Task Force. In particular, the Association suggested to the Committee that, "in addition to making the pre-bankruptcy and post-bankruptcy tax return available to creditors, a refund arising from any subsequent tax return filed during the bankruptcy should also be made available to creditors." It also believed that the discharge period should be extended to 15 months in order to allow the estate to benefit from the additional moneys from income tax refunds. The additional six months beyond the current nine-month period prior to discharge would also permit the trustee to offer additional counselling.

The Committee feels that clarification of the term "total income" is needed, and that trustees should be provided with guidelines to assist them in properly allocating lump-sum entitlements between debtors and creditors. Key definitions such as "total income" must have a clear and appropriate meaning, and trustees must be provided with guidance in order to ensure transparency, fairness, consistency and predictability in their dealings with debtors and creditors. Moreover, to the extent that is equitable, tax refunds payable to the debtor must be available to the trustee for distribution to creditors. We want the bankrupt to have a fresh start, certainly, but it is also important to us that proper consideration be given to maximizing assets in the estate in order that creditors receive more.

The Committee stresses the importance of ensuring adequate recovery for creditors not because we feel the need to be their advocate, but rather because inadequate recovery for creditors can have negative consequences, including a lower availability of credit and credit available only at a higher cost.

The Committee stresses the importance of ensuring adequate recovery for creditors not because we feel the need to be their advocate, but rather because inadequate recovery for creditors can have negative consequences, including a lower availability of credit and credit available only at a higher cost. These consequences have implications for the prosperity of the Canadian economy and, in fact, any Canadian who is forced to pay a higher cost of credit. Believing that clarity and

guidance are needed, and that these will result in greater fairness and predictability, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended in order to clarify the meaning of the term "total income." As well, clarity – in the form of guidelines contained in a directive of the Superintendent of Bankruptcy – should be provided to trustees regarding the manner in which lump-sum settlements received after bankruptcy and before discharge should be divided between debtors and creditors. Finally, a bankrupt's tax refunds received during a period to be determined by statute should be made available to the trustee for distribution to creditors.

H. The Definition of Consumer Debtor

In order to file a consumer proposal, an insolvent debtor must fall within the definition of "consumer debtor." A consumer debtor is a "natural person who is bankrupt or insolvent and whose aggregate debts, excluding any debts secured by the person's principal residence, do not exceed seventy-five thousand dollars or such other maximum as prescribed." The definition does not restrict the nature of the debts; they may be business- or consumer-related.

The $75,000 liability threshold, however, may be prompting many self-employed individuals and higher-income debtors to use the more complex and costlier option.

When the consumer proposal provisions were included in the BIA in 1992, it was expected that the administration of consumer proposals would be relatively straightforward and would not warrant the more complex and costlier option provided for commercial reorganizations. The $75,000 liability threshold, however, may be prompting many self-employed individuals and higher-income debtors to use the more complex and costlier option.

In the view of the Personal Insolvency Task Force, the current definition of "consumer debtor" is too restrictive, and the more complex process is not justified or needed for many of the debtors now using it. Higher costs reduce recovery for creditors, and failure of a commercial proposal results in automatic bankruptcy for the insolvent debtor; there is no "deemed bankruptcy" when a consumer proposal fails. It recommended that the BIA be amended to include a revised definition of "consumer debtor" for those filing a consumer proposal; it should include "an individual whose indebtedness, consequent of commercial or self-employed activity, does not exceed $100,000 or such other amount as is prescribed" and should include no ceiling on the amount of non-business indebtedness or on the debtor's assets.

Professors Ziegel and Telfer also supported a higher indebtedness threshold for consumer proposals, as did the Canadian Bar Association, which told the Committee that

"eligibility for consumer proposals should be enhanced, whether by raising the dollar ceiling from $75,000 to some higher figure, or in some other convenient manner." The Association, however, noted the absence of a provision in the consumer proposal scheme for payment of legal services rendered to the administrator and argued that "[s]ome provision must be made for the administrator to seek legal advice or representation. It is unfair to force the administrator to do so only at personal cost."

The general support by the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada for the Task Force's recommendations was augmented by their view that the proposed indebtedness threshold is too low. They believed that all debt should be classified together, since "it is difficult to distinguish between commercial and consumer debt … and consumer debts are frequently commingled with commercial debts for sole proprietors and small business owners, … ." From this perspective, they advocated an indebtedness threshold of $250,000 for all types of debt except residential mortgage debt.

A different view was shared with the Committee by the Canadian Bankers Association, which did not support the Task Force's recommendation to increase the indebtedness threshold for debtors filing a consumer proposal. It believed that "[i]ncreasing the threshold would increase the consumer debt to a level that was beyond that which a consumer could reasonably handle for payments under a proposal." Nevertheless, the Association informed us that, in the event that a decision is made to amend the BIA to increase the indebtedness threshold, it should be raised only in accordance with increases in the cost of living.

… *the Committee believes that consumers should pursue a consumer proposal rather than a commercial reorganization, if possible.*

Like a number of our witnesses, the Committee believes that consumers should pursue a consumer proposal rather than a commercial reorganization, if possible. We hold this view because failure in the former situation does not result in a "deemed bankruptcy," while in the latter case it does. Moreover, the consumer proposal option should be

Clearly, accessibility is hampered if the indebtedness threshold needed to access the simpler, less costly process is a barrier.

pursued because it is simpler and less costly. We recognize, however, that the current indebtedness threshold may be limiting the extent to which consumers are eligible to pursue a consumer proposal. One of the fundamental principles articulated by us in Chapter Two is accessibility. Clearly, accessibility is hampered if the indebtedness threshold needed to access the simpler, less costly process is a barrier. It is from this perspective that the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to raise the indebtedness threshold contained in the definition of "consumer debtor" to $100,000, with annual increases thereafter to reflect increases in the cost of living as measured by the Consumer Price Index. Moreover, two years after the new indebtedness threshold comes into force, the federal government should initiate a review of the degree to which insolvent debtors are using the consumer proposal option rather than pursuing a commercial reorganization. (page 184)

I. Selection of the Bankruptcy Trustee

At present, the BIA requires the Official Receiver to select a trustee to administer a bankruptcy; to the extent possible, this selection is required by law to reflect the wishes of the most interested creditors. In reality, however, in most cases the debtor chooses a trustee to administer his or her bankruptcy; it is rarely the case that the Official Receiver determines that a different trustee should be appointed.

The Personal Insolvency Task Force believed that the BIA should be amended in a manner that reflects the current reality with respect to trustee selection. The Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada supported this position, and told the Committee that the BIA should "be amended to reflect that in most cases, the debtor has initially selected the trustee to administer the bankruptcy."

The Committee completely agrees with the notion that legislation should reflect reality in those situations where the reality appears to be working well for all stakeholders.

The Committee completely agrees with the notion that legislation should reflect reality in those situations where the reality appears to be working well for all stakeholders. The situation regarding the selection of the trustee by the debtor rather than by the Official Receiver is an illustration of this point. In some sense, the fundamental principle of effectiveness appears to be well-served. For this reason, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to provide that the debtor is required to submit to the Official Receiver his or her choice of a trustee to administer his or her bankruptcy.

J. Non-Arm's Length Creditor Voting Rights

At present, the voting rights of creditors in a bankruptcy, who have been dealing with the debtor at non-arm's length in the year prior to the bankruptcy, are restricted by the BIA. This restriction applies to relatives of the debtor, as well as to other creditors who do not deal at arm's length. The concept of "arm's length" is borrowed from the *Income Tax Act* definition of that term. The BIA establishes a presumption that people who are related, within the meaning of the definition of "related" in the BIA, never deal at arm's length. The Court has the right to restore the voting rights of non-arm's length creditors if they represent more than 80% of the value of the total claims.

Non-arm's length creditors can never vote in favour of a proposal, although they may vote against acceptance of the proposal.

… the provision is predicated on the notion that collusion with the bankrupt is more likely to occur with non-arm's length than with arm's length creditors.

Designed to impede collusion between the bankrupt and a non-arm's length creditor that would undermine the interests of other creditors or that would give an advantage to a relative or other non-arm's length party, the provision is predicated on the notion that collusion with the bankrupt is more likely to occur with non-arm's length than with arm's length creditors. There may be situations, however, where this situation is unlikely; consider, for example, spouses involved in litigation. Until one year after a divorce is finalized, the non-arm's length estranged spouse is not permitted to vote as a creditor if his or her claim is less than 80% of the total claim; in the event that it is, Court approval is required in order to vote.

In the opinion of the Personal Insolvency Task Force, the BIA should be amended to: remove the 80% requirement so that, subject to Court approval, a non-arm's length creditor could vote at a creditor's meeting; and permit non-arm's length parties to appoint inspectors, subject to Court approval. The

Canadian Bar Association informed the Committee that it supported the Task Force's recommendations.

The Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada shared with the Committee their qualified support for the Task Force's recommendation. In particular, they believed that the vote should proceed prior to seeking leave of the Court; if the non-arm's length creditor's vote changes the outcome, the creditor should then seek leave of the Court to have the vote counted. They believed that a similar modification to the Task Force's recommendation is needed with respect to the vote to appoint inspectors. Finally, they told us that "the definition of 'non-arm's length' and 'related' [should] be clarified, to make the BIA more accessible for those wishing to participate."

The Committee feels that a premise on which this provision was designed may be faulty, since it implicitly assumes that collusion is significantly more likely to occur between the debtor and a non-arm's length creditor than between the debtor and an arm's length creditor. We think that this premise explains both the 80% threshold and the requirement to seek leave of the Court prior to participating in a vote. While we believe that there is some chance – and perhaps even a good chance – that collusion between the debtor and a non-arm's length creditor may occur, we believe that the premise is faulty in the sense that it perhaps occurs much less frequently than might commonly be thought. Certainly, although we lack data to support our view, we think that its frequency does not justify the relatively onerous nature of the provision as it is currently drafted.

While we believe that there is some chance – and perhaps even a good chance – that collusion between the debtor and a non-arm's length creditor may occur, we believe that the premise is faulty in the sense that it perhaps occurs much less frequently that might commonly be thought.

The Committee, in deciding whether this provision should be amended – and, if so, how – returned to the fundamental principles articulated in Chapter Two. We first put the current provision through the lens – if you will – of fairness, accessibility, predictability, efficiency and effectiveness. The provision failed to meet the standard expected in a number of areas. Change, then, is needed.

We also feel that the proposal for voting by the non-arm's length creditor, to be followed by a request to the Court if the vote changes the outcome, is wise and we endorse this approach.

Of the options presented to us by witnesses, the Committee believes that a change to the 80% threshold should occur, but do not believe that the elimination proposed by the Task Force is wise; in the absence of data about the extent to which collusion occurs, complete elimination may be too extreme and may have implications for the extent to which the Courts would be required to hear requests for the restoration of voting rights. Instead, we believe that it should be lowered, with a subsequent examination of the consequences of the reduction as a means of assessing whether additional change is required. We also feel that the proposal for voting by the non-arm's length creditor, to be followed by a request to the Court if the vote changes the outcome, is wise and we endorse this approach. Feeling that the changes we suggest will help to ensure fairness and accessibility for non-arm's length creditors, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to provide voting rights to non-arm's length creditors who have been dealing with the debtor at non-arm's length in the year prior to the bankruptcy, if they represent together more than 40% of the value of the total claims. In the event that the non-arm's length creditors vote changes the outcome of the vote, any interested party should then seek leave of the Court to have the vote included.

K. Debts Not Released by an Order of Discharge

Certain debts are not released by an order of discharge from bankruptcy, including "any debt or liability for obtaining property by false pretences or fraudulent misrepresentation." Sections 178(1)(d) and (e) of the BIA address some debts that are not released through discharge.

Some creditors have tried to invoke section 178 in order to prevent their claims from being discharged by arguing that an allegation of fraud is all that is required; that is, there is no requirement that fraud be proven to have occurred. As well, Section 178(1)(d) covers theft by a fiduciary, but does not cover theft by a stranger. Furthermore, Section 178(1)(e) applies to debts for property obtained through false pretences or fraudulent misrepresentation; debts for services obtained by improper means are not included.

The Personal Insolvency Task Force believed that these Sections of the BIA should be modernized. In particular, it argued that an allegation of fraud is insufficient and that a Court finding of fraud is required in order for the debt to survive discharge, and that debts for services obtained through false pretences or fraudulent misrepresentation should be covered in order to recognize the importance of services in our economy. Finally, it said that all theft should be covered, since there is "no policy reason to include only theft by a fiduciary … ." This recommendation was supported by the Canadian Bar Association, as well as by the Canadian Association of Insolvency and Restructuring Professionals and the Insolvency Institute of Canada.

In the Committee's view, the witnesses made a compelling case for amendment of Section 178 of the BIA.

Professors Ziegel and Telfer recommended that all of the non-dischargeable debts and penalties in Section 178 be reviewed.

In the Committee's view, the witnesses made a compelling case for amendment of Section 178 of the BIA.

… the provisions should apply to debts for services obtained through false pretences or fraudulent misrepresentation, as well as debts for property.

We, too, believe that fraud should be proven rather than merely alleged in order for the debt to survive discharge. As well, the provisions should apply to debts for services obtained through false pretences or fraudulent misrepresentation, as well as debts for property. In our opinion, changes of this nature would contribute greatly to fairness in the process. From this perspective, the Committee recommends that:

The *Bankruptcy and Insolvency Act* be amended to require that fraud be proven in order for a debt to survive discharge from bankruptcy. Moreover, the provisions should apply to both debts for property and debts for services acquired through false pretences or fraudulent misrepresentation.

CHAPTER SEVEN: CONCLUSION

Throughout our hearings, the Committee pondered the question of how "fresh" the "fresh start" should be for debtors, whether consumers or corporations. An answer to this question requires careful consideration of the balance that must be struck between providing honest but unfortunate debtors with an opportunity to be discharged from their debts and thereby begin again to contribute to society in a relatively unencumbered manner and the right for creditors of all types to recover as much as possible of the moneys owed to them and to share the burden of any shortfall in an appropriate manner. This philosophy is the fundamental premise on which Canadian insolvency law has evolved.

The answer, then, is: the fresh start should not be so fresh that creditors – whether suppliers of goods and services, grantors of credit or providers of labour – are unduly disadvantaged in the extent to which they can recover moneys owed to them, and thereby continue to provide goods, services, credit and labour with a reasonable expectation that they will be paid; but nor must the fresh start be so stale that debtors are unable, following discharge of their bankruptcy, to participate meaningfully in economic life because their non-dischargeable debt is overly burdensome for them. In the end, the true challenge is finding that elusive balance, recognizing that re-balancing is required from time to time as the domestic and international environments within which we live and do business change.

In this report, the Committee has provided recommendations that we believe will help to ensure opportunities for consumers and corporations to avoid bankruptcy – and thereby maximize opportunities for their personal or corporate recovery – and to share the burden of loss equitably should bankruptcy be unavoidable – and thereby allocate the burden fairly. This task is not easy. There are inherent conflicts and the problem is a "zero sum game." Most

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generally, improving recovery for one stakeholder occurs only at the expense of one or more other stakeholders.

A bankruptcy occurs because a debtor has insufficient assets to satisfy the claims of a range of creditors; in its simplest terms, there are inadequate resources available to pay debts as they become due.

By definition, insolvency involves opposing and competing interests. A bankruptcy occurs because a debtor has insufficient assets to satisfy the claims of a range of creditors; in its simplest terms, there are inadequate resources available to pay debts as they become due. The Committee was mindful of the changes over time that have diminished the moneys available for recovery by creditors. Consequently, in our recommendations we were cautious in recommending additional exemptions from seizure in bankruptcy and discharge of debts that would further reduce these moneys and affect the balance between stakeholders.

Finally, the Committee believes that review must be ongoing, for insolvency legislation must respond to the changing domestic and global socio-economic environment. Our report – and the legislation that we expect will follow – are movements along the road. It is our hope that we will continually travel this road but never arrive at the end of it, for it is the continuous travel that reflects the change that must always occur in order to ensure that our insolvency regime is the best that it can be and that it continues to meet the often-conflicting needs of stakeholders in the fairest and most accessible, predictable, responsible, cooperative, efficient and effective manner possible.

APPENDIX A:
THE *WINDING-UP AND RESTRUCTURING ACT* AND THE *FARM DEBT MEDIATION ACT*

A. The *Winding-up and Restructuring Act*

Enacted in 1882, the *Winding-Up Act* (WUA) provided a process for the liquidation of both solvent and insolvent corporations. With the passage of the *Bankruptcy Act* in 1919, a second regime for liquidating insolvent companies was created, and the *Bankruptcy Act* was made paramount with amendments in 1966 that had the effect of limiting the WUA's application to the winding-up of certain financial institutions. In that year, the Minister of Justice initiated a major reform process with respect to insolvency law; part of this process involved the establishment of the Study Committee on Bankruptcy and Insolvency Legislation, or the Tassé Committee.

When the Tassé Committee reported in 1970, it proposed that the *Bankruptcy Act* and the *Winding-Up Act* – to the extent that the latter applied – be merged in a single bankruptcy statute applicable to the liquidation of all insolvent companies. Although a number of legislative proposals that would have enacted a comprehensive insolvency statute and repealed provisions related to insolvent corporations in the WUA have been considered since that time, no merger of the WUA and the *Bankruptcy and Insolvency Act* has occurred. In recent years, the *Winding-Up Act* has been amended to facilitate the liquidation of financial institutions and to rename the Act.

At the present time, the *Winding-Up and Restructuring Act* (WURA) applies to insolvent financial institutions, such as banks, insurance companies, trust companies and loan companies; these companies cannot be liquidated under the *Bankruptcy and Insolvency Act*, and the WURA's provisions have been tailored to address the unique circumstances associated with administering the liquidation of insolvent financial institutions. The Act also applies to a range of solvent companies that wish to be wound up; however the federal *Canada Business Corporations Act* (CBCA) excludes the WURA's application to CBCA corporations, and other federal and provincial/territorial incorporations legislation may also do so. Consequently, most – although not all – solvent companies can be wound up under other legislation as well, including liquidation and dissolution provisions or federal and provincial/territorial corporations legislation and provincial/territorial winding-up legislation.

Different in both structure and procedure from the BIA, proceedings under the WURA are largely Court-driven. A liquidator is appointed by the Court to carry out the day-to-day administration of the process, and the Court must approve all key decisions made by the

liquidator. The Act requires the liquidator to take possession of the company's property, wind up its business and distribute the assets to creditors.

The Act provides two categories of preferred claims: a portion of the claims of employees for wages, and claims for the costs of administration. Moreover, since the Crown is not bound by the WURA, it is in a relatively stronger position to pursue its claims. Finally, the Act lacks rules governing international insolvencies and provides a relatively limited reorganization regime. In particular, the Act authorizes the Court to call a meeting of creditors in order to vote on a reorganization proposal and allows the Court to make the proposal binding on all creditors provided 75% of the creditors in any class vote in favour of the proposal.

A number of practitioners and analysts have recommended that the *Winding-up and Restructuring Act* be amended. This Act is not subject to the current statutory Parliamentary review.

B. The *Farm Debt Mediation Act*

Under the *Farm Debt Review Act*, proclaimed into force on 5 August 1986, provincial Farm Debt Review Boards were established to ensure that farm operations in financial difficulty or facing foreclosure had access to impartial third-party review and possible financing or refinancing. Each Board identified persons available to serve on three-person Farm Debt Review Panels, which were established for each farm debt review to consider the financial affairs of the farmer and to facilitate an arrangement between him or her and his or her creditor(s).

Two types of applications were possible. In the case of an insolvent farmer, the Act required a secured creditor(s) to give the farmer at least 15 business days' notice of action being taken and of his or her right to make an application under the Act. The farmer was then able to apply to the Farm Debt Review Board, and the Board notified all creditors and issued a 30-day stay of proceedings against foreclosure; the stay could be extended at 30-day intervals for a total of 120 days if the Board felt that an extension of the period was essential to the formulation of an agreement between the farmer and his or her creditor(s). A Farm Debt Review Panel met with field staff, the farmer and his or her creditor(s) to assess the situation and to attempt to achieve a mutually satisfactory agreement. If successful, any agreement reached constituted a legal contract. In the event of failure, the creditor(s) were able to proceed with foreclosure.

A farmer in financial difficulty could apply to the Farm Debt Review Board for a review of his or her financial affairs or for assistance in reaching an agreement with his or her creditor(s). A Farm Debt Review Panel was established, and field staff were assigned to evaluate the situation with the farmer and, if requested by him or her, his or her creditor(s); preliminary suggestions for improving the farmer's prospects were made. After reviewing

the final report, the Panel met with the farmer and, if he or she so requested, his or her creditor(s), to discuss the report and to attempt to enter into an agreement. Any agreement signed became a legal document.

In May 1996, Bill C-38 was introduced in the House of Commons. It repealed the *Farm Debt Review Act* and enacted the *Farm Debt Mediation Act* (FDMA). The FDMA, which came into force in April 1998, implemented a simplified procedure that focuses on mediation and applies to insolvent farmers. In general terms, the Act provides for: a review of an insolvent farmer's financial affairs; mediation between the farmer and his or her creditor(s) with the objective of reaching a mutually acceptable arrangement; and, if requested by the farmer, an order temporarily suspending the right of his or her creditor(s) to take or to continue proceedings against the farmer's assets.

To be eligible to make application under the Act, a farmer must meet one of three criteria: to be unable to meet his or her obligations as they generally become due; to have ceased paying his or her current obligations in the ordinary course of business as they generally become due; or to have property the aggregate of which is not, at a fair market valuation, sufficient to enable payment of all of his or her obligations due. These criteria correspond to the definition of "insolvent person" in the *Bankruptcy and Insolvency Act*.

A farmer meeting one of these three insolvency criteria can make one of two types of applications: for a stay of proceedings against him or her by all creditors, a review of his or her financial affairs, and mediation between him or her and all creditors for the purpose of assistance in reaching a mutually acceptable arrangement; or for a review of his or her financial affairs and mediation between him or her and all secured creditors for the purpose of assistance in reaching a mutually acceptable arrangement, although one or more unsecured creditors can be involved in the mediation in certain circumstances. With the first type of application, the farmer has access to a 30-day stay of proceedings, which can be extended in some circumstances for up to three further periods of 30 days each and can be terminated under a variety of circumstances; during the period of the stay, a guardian of the farmer's assets is appointed. With permission, farmers can change their application from one type to the other at any time during the mediation. There is a duty on the administrator of the process to give notice of the application to each of the farmer's creditors in the first case or to secured creditors in the second case.

Following the financial review of the farmer's affairs, a single, neutral mediator is appointed to assist the farmer and any relevant creditors in reaching a mutually acceptable arrangement; the mediator neither advises farmers nor negotiates on behalf of either them or their creditor(s). In the first type of application, mediation ends when the stay of proceedings is terminated. Different restrictions apply in the second type of application. In particular, if the administrator of the process believes that the farmer or most of the creditors refuse to participate in good faith in the mediation, or that the farmer and most of the creditors will not reach agreement, then he or she can direct that the mediation be terminated. Mediation is also terminated on the signing of an arrangement between the farmer and any creditor.

Every secured creditor intending to enforce a remedy against a farmer's property or to commence any proceeding or action, execution or other proceeding for the recovery of a

debt, the realization of any security, or the taking of any of the farmer's property is required to give the farmer written notice of this and to advise him or her of the right to make an application under the *Farm Debt Mediation Act*. This notice is required at least 15 business days prior to taking any of the acts described.

During Parliamentary examination of Bill C-38, some commentators criticized the proposed process because it would not apply to farmers in financial difficulty, as had been the case under the *Farm Debt Review Act*. A Farm Consultation Service, however, is available as a complementary program to the *Farm Debt Mediation Act*. It provides confidential financial management counselling to farmers.

The Minister of Agriculture and Agri-Food undertakes a review of the operation of the Act every three years, and tables a report on the review before the Senate and the House of Commons. The most recent report was tabled on 13 June 2001 for the period of 1998 to 2000. There is no statutory Parliamentary review of the Act.

APPENDIX B:
THE EVOLUTION OF INSOLVENCY LEGISLATION IN CANADA WITH PARTICULAR REFERENCE TO THE *BANKRUPTCY AND INSOLVENCY ACT*

A. The Early Years

Canada's first federal insolvency statute was enacted by Parliament in 1869 with the passage of *An Act Respecting Insolvency*. This legislation covered voluntary and involuntary bankruptcies, provided for compositions and applied only to traders. Although the law was revised and consolidated in a new Act, the *Insolvent Act of 1875*, the legislative provisions did not have the intended effects and the law was repealed in 1880. Thereafter, for almost four decades Canada lacked a general bankruptcy law in force throughout Canada.

The situation changed with the 1919 *Bankruptcy Act*, which was modelled on the English statute of 1914. Major changes were not made, however, until three decades later, when a new *Bankruptcy Act* was passed in 1949. Nevertheless, some amendments were made during the 1919 to 1948 period. For example, in 1932 the Act was amended to establish the position of the Superintendent of Bankruptcy, and provision was made for the licensing of trustees.

B. The 1949 *Bankruptcy Act*

Legislation was introduced in 1949 to amend the *Bankruptcy Act* in order to attain several objectives:

- to provide a system of summary administration for small estates;
- to permit a debtor to offer, and creditors to accept, a proposal without the debtor going into – or being put into – bankruptcy;
- to clarify the priorities given to various classes of claims when distributing the debtor's assets; and
- to increase creditor control over a bankrupt's estate by vesting, in the creditors and inspectors, responsibilities and obligations for which they were previously required to resort to the Court.

Royal Assent was given in December 1949.

C. The 1966 Amendments

When amendments to the *Bankruptcy Act* were introduced in 1966, they were viewed as interim measures designed to address the most pressing issues, pending complete revision of the legislation. In particular, the *Bankruptcy Act* was amended in order to:

- provide more adequate means of addressing fraud connected with bankruptcies;
- enable the dissemination of information about bankruptcies so that creditors could better assess the credit rating of prospective clients;
- enable the Courts to review transactions that might not fall within what might be called "moral business practices;"
- tighten provisions related to proposals to give creditors better protection and to prevent a proposal from being used as a stalling device that would allow a debtor to dissipate his or her assets;
- require bankrupts to deposit, with their trustee for the benefit of creditors, a certain proportion of their salaries, wages or other remuneration;
- expand provisions dealing with offences by trustees; and
- prevent a bankrupt corporation from applying for a discharge.

The legislation received Royal Assent in July 1966.

D. The 1970s, Legislative Inertia and a Focus on Wage Earner Protection

A number of insolvency-related initiatives occurred in the 1970s, beginning with the publication of the report of the Tassé Committee. Formed in 1966 as the Study Committee on Bankruptcy and Insolvency Legislation, the Committee's task was to undertake an in-depth study of Canadian insolvency law. In its report, the Committee recommended that a completely new bankruptcy and insolvency statute be enacted that would establish an integrated and comprehensive system. The Committee believed that a new statute was needed in light of the economic and social changes that had occurred since the enactment of the *Bankruptcy Act* in 1949. The 113 recommendations made by the Committee focussed on such areas as: measures to facilitate the payment of debt; "the last resort solution;" liquidation outside bankruptcy; crime and the protection of the credit system; administrative issues; and the Courts. As well, an area for change identified in the Tassé Report was super priority status for unpaid wage claims up to $2,000, binding secured and general creditors.

Bill C-60 – intended to implement the recommendations of the Tassé Report – was introduced in the House of Commons on 5 May 1975 and, after first reading, was referred to

the Standing Senate Committee on Banking, Trade and Commerce. Following its study, the Committee recommended 139 changes to Bill C-60, and the Bill was permitted to lapse. One area in which the Committee recommended change was unpaid wage claims.

On 21 March 1978, Bill S-11 was introduced in the Senate. It contained 128 of the amendments to Bill C-60 that had been recommended by the Senate Committee. Although second reading occurred on 4 April 1978, the Bill was not passed. It was, however, re-introduced as Bill S-14 on 27 February 1979 and progressed to second reading before it died on the Order Paper when Parliament was dissolved on 26 March 1979.

Finally, Bill S-14 was re-introduced in the Senate on 8 November 1979 as Bill S-9. Following first reading, it too died on the Order Paper on 13 December 1979.

E. The 1980s and a Continued Focus on Wage Earner Protection

In 1980, the Committee on Wage Protection in Matters of Bankruptcy and Insolvency, chaired by Raymond Landry, was asked to make recommendations on wage protection. The Committee's report, published in October 1981, concluded that – in the absence of complete and accurate data on the number and value of unpaid wage earner claims – it was unable to determine the severity of the problem of unpaid wages. The limited evidence available did, however, indicate the existence of a problem.

In its report, the Landry Committee noted that the United Kingdom, France, West Germany, Belgium and Denmark had wage earner protection schemes, and recommended the same for Canada. In its view, however, a permanent legislative solution could not be drafted until the size of the problem had been determined and until federal and provincial/territorial policies had been coordinated. Consequently, the Committee recommended an interim three-year solution during which up to $1,000 in unpaid wages would be paid out of the Consolidated Revenue Fund.

On 16 April 1980, Bill C-12 was introduced in the House of Commons and was referred to the House of Commons Standing Committee on Finance, Trade and Economic Affairs following second reading. The Bill died on the Order Paper when Parliament was dissolved during the Committee's hearings, which did not begin until 1983.

Bill C-17, which was essentially the same as Bill C-12 except for the addition of technical amendments, was introduced in the House of Commons on 31 January 1984. Although additional amendments were tabled on 28 May 1984, the Bill died on the Order Paper after second reading. With respect to unpaid wage claims, the Bill provided that a claim for wages up to $4,000 would rank in priority over the claims of all secured creditors. The idea of a wage protection fund lacked support because of the absence of statistical data on the cost and the possibility that it would provide a disincentive to employers to pay wages on time.

In March 1985, the Minister of Consumer and Corporate Affairs established an Advisory Committee comprised of trustees and lawyers to examine the bankruptcy system, assess

possible reforms and recommend legislative amendments. The Committee's report – known as the Colter Report – was released in January 1986. The Report made 122 recommendations for change in such areas as: wage earner protection; receivers and secured creditors; commercial reorganizations; suppliers of merchandise; consumer bankruptcies and arrangements; preferred claims; farmers and fishers; securities firms, insurance companies and financial institutions; international insolvencies; estate administrative matters; and directors' and officers' liabilities.

With respect to wage earner protection, the Colter Report advocated the establishment of a fund, financed by employer and employee contributions, which would make certain payments to employees whose employers had been either declared bankrupt or put into receivership; payments would be made, to a maximum of $2,000, for wages and commissions, vacation pay and pension benefits, although amounts due as severance payments would remain as unsecured claims.

Following the release of the Colter Report, in September 1986 the Department of Consumer and Corporate Affairs released a discussion paper on amendments to the *Bankruptcy Act*, and provided a number of recommendations based on the findings of the Colter Report and on its consultations with stakeholders and the provinces/territories. In 1988, the Department released *Proposed Revisions to the* Bankruptcy Act, in which it proposed reforms in eight areas. This approach involved reform of certain key aspects of the law rather than the presentation of a completely new statute with far-reaching reforms.

The Department's report also addressed the issue of unpaid wage claims, but differed somewhat from the recommendations made in the Colter Report. In particular, the Department proposed that the program be financed by the federal government rather than by employer and employee contributions; it did, however, support the recommendation made in the Colter Report regarding a maximum monetary limit, although the extent to which unpaid wages and vacation pay would be covered differed between the proposals.

Finally, the issue of unpaid wages was also addressed in the March 1989 *Report of the Advisory Council on Adjustment* – also known as the de Grandpré Report – which examined adjustment issues arising as a consequence of the Canada-United States Free Trade Agreement. As part of its examination of employment issues in an age of globalization, the Report recommended amendments to the *Bankruptcy Act* that would create a national wage earner protection fund that would cover up to $4,000 in unpaid amounts owing to employees for wages, vacation pay, pension and benefit premiums, and severance pay. In the event that the fund was not created, the Report recommended that the federal government enact legislation, on an expeditious basis, to ensure that wage earner claims would have priority over all other claims in the disposition of assets of an insolvent employer.

F. Bill C-22: The 1992 Changes

Bill C-22 was introduced in the House of Commons on 13 June 1991 and its provisions came into force on 30 November 1992. The Bill was designed to:

- achieve a better balance between the rights of various categories of creditors as well as between the rights of creditors and debtors;
- enable individuals and businesses to reorganize their financial affairs in an effort to avoid bankruptcy; and
- make the laws more effective, less costly and easier to apply.

Principal areas of reform contained in the Bill included:

- wage claims, although this proposal was subsequently withdrawn;
- secured creditors and receivers;
- commercial reorganizations;
- consumer proposals, including mandatory counselling in order to receive a nine-month unconditional discharge;
- Crown claims and priorities;
- protection for unpaid suppliers; and
- technical amendments.

The Bill also introduced the concept of insolvency into the title of the legislation, and required Parliamentary review after three years.

G. Bill C-5: The 1997 Changes

Anticipating the three-year statutory review that had been included in the 1992 *Bankruptcy and Insolvency Act* (BIA), the federal government established the Bankruptcy and Insolvency Advisory Committee, comprised of government and private sector representatives, to examine various areas of bankruptcy law and to make recommendations for change. Many of the Committee's recommendations were included in Bill C-5.

Introduced in the House of Commons on 4 March 1996, Bill C-5 was essentially the same as Bill C-109, which had been introduced in the House of Commons on 24 November 1995 but died on the Order Paper following first reading.

As introduced in the House of Commons, Bill C-5 proposed to amend the BIA with respect to:

- the licensing and regulation of bankruptcy trustees;
- the liability of trustees for environmental damage and claims;
- the liability of directors and stays of action against directors during reorganizations;
- compensation for landlords where leases are disclaimed in a reorganization proposal;
- procedures in consumer proposals;
- consumer bankruptcies;
- the dischargeability of student loan debt;
- Workers' Compensation Board claims;
- codification of requirements for bankrupts to contribute part of their income to the bankruptcy estate;
- international insolvencies; and
- securities firm insolvencies.

The Bill also proposed amendments to the *Companies' Creditors Arrangement Act* (CCAA) in order to align more closely the provisions of the CCAA and the BIA. It did not, however, address such issues as the rights of unpaid suppliers and a wage earner protection fund.

After consideration in the House of Commons, the Bill was studied in the Senate by the Standing Senate Committee on Banking, Trade and Commerce. In February 1997, the Committee issued a report on the Bill and recommended a number of amendments; Bill C-5, as amended, received third reading in the Senate in February 1997. On 15 April 1997, the House of Commons concurred in the Senate amendments, and the Bill received Royal Assent on 25 April 1997. Provisions came into force in September 1997 and April 1998.

H. Bill C-36: Student Loan Debt

Bill C-36, An Act to implement certain provisions of the budget, was introduced in the House of Commons on 24 February 1998 and proposed amendments to the *Bankruptcy and Insolvency Act*, among other Acts. As part of a package of changes related to the financing of post-secondary education – which included provisions related to interest relief – the Bill proposed that student loan debt not be dischargeable where bankruptcy occurs within ten years after the completion of studies; prior to this change, the period was two years.

I. The Current Insolvency Process: Consumers

At present, individuals who find themselves with an unmanageable debt burden have several options available to help them return to financial health. For example, these individuals might consider: a debt consolidation loan; an informal proposal with creditors; or, in some provinces/territories, a Consolidation Order setting out the amount and times when payments are due to the Court, which then distributes payments to creditors on behalf of the debtor. In Quebec, the Voluntary Deposit scheme – or Lacombe Law – is similar to a Consolidation Order.

In addition to these options, an insolvent debtor may consider bankruptcy or the making of a proposal. In order to meet the definition of insolvency, the individual must: owe at least $1,000 and be unable to meet his or her debts as they are due to be paid; have ceased paying his or her current obligations in the ordinary course of business as they generally become due; or have property the aggregate of which is not, at a fair market valuation, sufficient to enable payment of all of his or her obligations due.

Under the *Bankruptcy and Insolvency Act*, a trustee or an administrator may file a consumer proposal, which is a proposed agreement between the debtor and his or her creditors whereby the parties agree that the debtor will pay off a portion of his or her debt, that the time period over which the debt will be paid will be extended, or that some combination of both of these will occur; in essence, it involves restructuring the payment obligations. The trustee is required to provide the creditors with a report on the affairs of the debtor, the causes of the financial difficulties, and an estimate of what the creditors would realize under a bankruptcy as compared with the amount offered under the proposal.

Two types of proposal are possible: a consumer proposal where the debtor's aggregate debt, excluding debt secured by a principal residence, does not exceed $75,000 and the proposal includes a maximum five-year debt repayment scheme; or a proposal, available as an option for individuals regardless of their level of indebtedness and for corporations. If creditors fail to accept the first type of proposal, the debtor is not automatically bankrupt; with the second type of proposal, however, failure by the creditors to accept the proposal results in the debtor becoming bankrupt.

In order for a proposal to be acceptable to creditors, it must generally be the case that they would be better off – as a result, for example, of quicker distribution, lower administrative costs, a higher level of payment or a more certain outcome of issues – than they would be if the debtor were to become bankrupt. Thus, since 1992 when the option of consumer proposals was added to the BIA, proposals have been seen by many as a win-win situation: creditors gain because they are better off than they would be if the debtor were bankrupt, and the debtor avoids bankruptcy. The growth of proposals as an alternative to bankruptcy has been particularly rapid since 1997, although one might have expected relatively rapid growth following the enactment of the proposal option in 1992.

If creditors vote in favour of a proposal – which requires that the proposal be approved by at least 66.6% in dollars and 50% plus one in number of eligible creditors who vote – then it

is approved by the Courts and is a contract that is binding on all creditors. The debtor retains control of his or her assets, except where the proposal stipulates otherwise.

In the event of a debtor's bankruptcy – whether it occurs voluntarily or, more rarely, as a result of creditors asking the Court to order that a person is bankrupt – certain property is exempt from seizure. The range and value of exempt property varies across provinces/territories, although apparel, household furnishings, one vehicle, professional tools and books, and medical devices are generally exempt to certain limits. Funds in registered pension plans and life insurance Registered Retirement Savings Plans are also exempt. Assets held by the bankrupt or acquired by the bankrupt during the period of bankruptcy that exceed these exemptions vest with the trustee, who will dispose of the non-exempt assets for the benefit of the bankrupt's creditors.

Individuals who are bankrupt for the first time receive an automatic discharge after nine months, provided the creditors, the Superintendent of Bankruptcy or the trustee do not oppose the discharge and the bankrupt has undergone mandatory counselling; with the 1992 amendments to the BIA, Canada became the first country to make financial counselling mandatory prior to an unconditional discharge. The discharge cancels the bankrupt's debts, with certain exceptions, including child support payments, alimony payments, Court-imposed fines and student loan debts if the bankruptcy occurs within ten years after the completion of studies. The bankruptcy remains on the individual's credit record for six years.

J. The Current Insolvency Process: Corporations

Insolvent corporations have a number of options, including reorganization or bankruptcy. Reorganization can occur under either the *Bankruptcy and Insolvency Act* or the *Companies' Creditors Arrangement Act,* although a $5 million debt threshold must be met if the corporation elects to proceed under the CCAA.

In the case of reorganization, a trustee files a proposal with the organization's creditors, who are more likely to accept a proposal if they are better off with the reorganization of the business than they would be if the company were to become bankrupt. Proposals for reorganization typically involve the organization paying off only a portion of its debts and/or paying its debts over a longer period of time, or both. This circumstance is viewed as a potentially win-win situation: the organization remains in business, workers continue to be employed, and creditors both retain a customer and receive at least a portion of the moneys owed to them.

The trustee must provide creditors with a report on the financial affairs of the company, the causes of the organization's financial difficulties and an estimate of the amount creditors would realize under a bankruptcy as compared with the amount being offered under the reorganization proposal. The proposal must include provision to pay both employee source deductions outstanding within six months after Court approval, and outstanding wages and

vacation pay owed to employees and former employees, up to a maximum of $2,000 each, immediately after Court approval.

Organizations can be placed into bankruptcy through a number of circumstances: a creditor petitioning the company into bankruptcy (a Court proceeding); the company's directors filing an assignment of the company; defeat of a proposal at the meeting of creditors; refusal of the Court to ratify a proposal which had been approved by the creditors; or annulment of a proposal as a result of non-performance. In these circumstances, a trustee acquires control of the organization's assets that remain following enforcement by secured creditors and liquidates them for the benefit of unsecured creditors.

APPENDIX C:
THE REPORT BY INDUSTRY CANADA

In the *Report on the Operation and Administration of the* Bankruptcy and Insolvency Act *and the* Companies' Creditors Arrangement Act (hereafter, the IC report or the report), Industry Canada presents the issues raised and conclusions reached during its consultations with stakeholders in three areas: administrative policy issues; commercial insolvency issues; and consumer insolvency issues.

A. Administrative Policy Issues

In general, stakeholder comments on administrative policy issues focussed on the needs of the Office of the Superintendent of Bankruptcy (OSB) in order to administer the system effectively, and on impediments that can be removed or minimized.

1. Volume, Access and Funding

The IC report notes the continued growth in the number of insolvency files in recent decades, and questions whether preventive approaches should be adopted to halt this trend and to encourage debtors to adopt credit management practices that would reduce the likelihood of insolvency.

It also suggests that, because of the costs associated with entering into bankruptcy, low-income debtors may be unable to access the system. In particular, if a trustee believes that it may be difficult to collect the fees for services rendered, he or she may require an advance or security as a condition of accepting the assignment; this situation could be a barrier to access for some debtors. Nevertheless, the Bankruptcy Assistance Program established by the Office of the Superintendent of Bankruptcy (OSB) facilitates access, since trustees voluntarily provide services at no charge to debtors unable to afford the services of a trustee. The IC report questions whether universal access to bankruptcy services should be redefined, with new measures to ensure access, or whether access should cease to be seen as a right.

Moreover, the report notes that, since becoming a Special Operating Agency, the OSB depends on income generated by its operations to fulfill statutory obligations. The Office must ensure compliance with the *Bankruptcy and Insolvency Act* (BIA) within its budgetary limits, which is increasingly difficult with a rising number of files received each year. A number of options exist for increasing OSB funds, including the identification of new bases of revenue and higher fees. Also mentioned in the IC report is the contribution that new

technology can make in enhancing the efficiency of the system for all users; almost 80% of the Office's services are currently available electronically and all services are likely to be available electronically by 2004, which means that there are limited opportunities for cost savings in this area. Nevertheless, amendments to the BIA may be required to provide more clearly for electronic transactions.

2. The Debtor Compliance Program

In order to prevent abuse and maintain the public's trust in the integrity of the insolvency system, an effective program is needed to ensure debtor compliance with the BIA; the need may be particularly acute in light of growing caseloads, more complex cases and increasingly scarce resources. The IC report questions whether the BIA should be modernized and reviewed to determine if certain offences would be better addressed through civil and/or administrative remedies, rather than through criminal proceedings.

3. Regulatory Supervision of Reorganizations under the *Companies' Creditors Arrangement Act*

Unlike the BIA, the *Companies' Creditors Arrangement Act* (CCAA) is not subject to any administrative supervision and there is no centralized public record of CCAA reorganizations. Consequently, it is difficult to assess – in any meaningful or verifiable manner – the extent to which reorganization plans are effective and to which the CCAA's provisions are being applied and administered consistently; one consequence of this lack of supervisory process could be reduced trust by lenders and investors. Moreover, the monitors appointed to monitor the affairs and finances of a business during its reorganization are not bound by rules of professional conduct and are not subject to qualification requirements.

In light of the social and economic importance of reorganizations under the CCAA and the increasing frequency with which they occur, the IC report questions whether a supervisory regime would be appropriate in order to provide: a national and public registry; mechanisms to address complaints; the power to intervene in Court proceedings; and licensing requirements for monitors.

4. Regulatory Supervision of Receiverships

According to some stakeholders, the provisions in the BIA that govern receiverships have not been effective and are not being used in the manner intended. The provisions apply when a secured creditor or its agent – a receiver – takes possession of all or substantially all

of the assets of a business to realize them for the secured creditor's benefit. The IC report notes a number of deficiencies with these provisions, including the definition of "receiver," a restrictive interpretation of the provisions by common law Court, and inadequate penalties for those who do not comply with the provisions.

5. Consolidation of Insolvency Statutes

As part of its examination of corporate insolvency issues, the IC report addresses the concept of whether the BIA and the CCAA should be integrated. Here, the concept is presented as an administrative policy issue rather than a corporate insolvency concern because integration of the statutes could involve Superintendent of Bankruptcy oversight over the merged law.

The IC report notes that the existence of these separate insolvency statutes is a consequence of historical circumstances, and indicates that stakeholders hold various opinions about whether the BIA and the CCAA should be merged and, if so, to what extent. It also comments on the lack of data regarding the use and application of the CCAA, which limits meaningful debate on the issue.

B. Commercial Insolvency Issues

Stakeholders identified a range of commercial insolvency issues during the consultation process. While they were able to reach consensus on some issues – including securities firm bankruptcies, the *Winding-up and Restructuring Act*, financial market issues, and trustee liability for successor employer obligations and pension claims – other issues remained unresolved because of significant or extreme differences of opinion among stakeholders. The unresolved issues included: wage earner and pension protection; Debtor-in-Possession (DIP) financing; unpaid supplier rights; adoption of the UNCITRAL Model Law on Cross-Border Insolvency; contractual rights; integration of the BIA and the CCAA; director liability; sanctions for director and officer conduct detrimental to creditors; and transfers at undervalue and preferences.

1. Compensation Protection: Wages and Pensions

The extent to which the wage and pension income of employees is protected in insolvency proceedings is a longstanding concern in Canada, and while some wage protection has existed since 1949, the issue has been examined repeatedly since the 1970s. The IC report describes the various legislative and other proposals that have been discussed over time to protect wages, including: preferred-claim status and the maximum amount that is

appropriate; super priority protection; a wage protection fund financed by some combination of employers, employees and the Consolidated Revenue Fund; and protection through the employment insurance system. It raises questions about the distributional effects of compensation protection, and about the impact of such measures on economic activity and efficiency as well as on credit availability and cost.

Moreover, the IC report identifies concerns about the extent to which existing protection for unpaid contributions to – and unfunded liabilities of – pension plans is adequate and, if inadequate, how the protection might be improved. At the present time, Ontario is the only jurisdiction that provides funded protection for pension claims, although bankruptcy legislation tabled in the 1970s and 1980s, as well as a number of advisory committees, have commented on such issues as priority for pension claims and the establishment of a fund to cover pension claims.

2. Debtor-in-Possession Financing

Debtor-in-Possession (DIP) financing assists insolvent businesses that need financing in order to reorganize; since this type of lending is usually risky, lenders may require that they have priority over other secured creditors. The BIA and the CCAA are silent on the issue of DIP financing, although Canadian judges – using their inherent jurisdiction – have authorized such financing in CCAA cases.

The IC report notes concerns by stakeholders about whether DIP financing should: have a legislative basis; be imposed on creditors without further defining the circumstances under which it is warranted; and rank ahead of existing creditors. Another concern is that insolvent companies – which may have financial and management difficulties – may not succeed even with DIP financing, a situation that would result in even greater loss than would otherwise be the case. The absence of data regarding the success of reorganizations under the CCAA – and the role that DIP financing may play in that success – limits meaningful debate on this issue.

3. The Rights of Unpaid Suppliers

Stakeholders have concerns about the effectiveness of the protection for unpaid suppliers, or the "30-day goods rule," which has existed in the BIA since 1992. In particular, the IC report identifies concerns about: the fact that the 30-day recovery period begins on the date of delivery rather than the date of the debtor's initiation of bankruptcy; the limitation requiring that recovery be limited to goods that are in the same state as when they were delivered; and the application of the provisions to the supply of goods but not of services.

4. Cross-Border Insolvencies

UNCITRAL – the United Nations Working Group on Insolvency Law – has recommended that countries adopt, as part of their domestic insolvency law, its Model Law on Cross-Border Insolvency. Adoption of the Model Law in Canada would involve replacing parts of the BIA adopted in 1997 in response to increasing globalization and the rising number of insolvencies that are international in nature. The IC report notes that adoption of the Model Law would assist international harmonization efforts regarding the treatment of international insolvencies, with more uniform interpretation of rules and easier administration of international insolvencies.

The IC report reflects stakeholder questions about whether: Canada should adopt a reciprocity provision if it adopts the Model Law; adopting the Model Law could reduce the number of insolvency cases heard in Canada; the Model Law should be adopted as written, or adopted with modifications; and Canada should adopt select Model Law features and add them to existing provisions in the BIA.

5. Contractual Rights

The IC report questions whether – and, if so, the extent to which and in what circumstances – insolvency law should intervene in private contracts in order to ensure fair distribution or maximization of value in an insolvency, recognizing that contracts contain terms negotiated in good faith and reflective of risks. The report notes stakeholder concerns about whether: secured creditors should be temporarily stayed from enforcing their rights in bankruptcy; the BIA requires rules governing leases; and existing intellectual property rights reflect the competing interests of various parties.

Allowing intervention in contractual rights is likely to affect contractors' expectations, reduce predictability, lower certainty in contracting and increase risk. The report suggests that, in this context, the benefits of intervention should be assessed against the costs of such intrusion. Situations cited in the report to illustrate the desirability of continuing a contract include: allowing a trustee to use leased premises for a period of time while assets are being evaluated and liquidated; and the continued use of software under licence that may be integral to a business. While it may be the case that "valuable" contracts should be allowed to survive, creditors and debtors may not always agree on which contracts are "valuable."

6. Directors: Liability and Sanctions

On the issue of directors' liability, the IC report questions whether existing rules in this area strike the appropriate balance between attracting competent directors and creating a sufficient obligation to ensure that they act diligently in the performance of their duties.

While federal and provincial/territorial laws provide that directors are exposed to personal liability for a number of corporate debts, in most cases they have access to due diligence or good faith defences; in other cases, however, they are subject to absolute liability and have no defence.

The report notes that reduced exposure by directors to personal liability could encourage competent individuals to accept positions as directors, and to remain as directors when their companies are insolvent. Nevertheless, reduced exposure would lower the incentive for directors to ensure that payments are made to wage earners and others protected by directors' liability provisions. A number of options for reform are presented, including: placing directors' liability for wages directly in the BIA, with a due diligence defence; allowing directors to be exonerated from liability for claims arising in the period immediately prior to or after insolvency proceedings are commenced; and focussing efforts on identifying – and taking action against – wrongdoing by directors, but otherwise allowing them to be blameless in insolvencies.

The IC report also comments on sanctions for director and officer conduct detrimental to creditors. There is some concern about whether the existing sanctions for inappropriate conduct are properly balanced with ensuring diligent performance while encouraging competent persons to act as directors, and about whether sanctions are effectively enforced. At the present time, directors may be held personally liable for failure to consider creditors' interests when their companies become insolvent.

Although the report notes that recent case law has resulted in directors and officers taking fewer risks in their efforts to revive insolvent companies, it questions whether director disqualification provisions might be effective in identifying incompetent directors and reducing abuse; such provisions could, however, be costly to enforce effectively and could have negative implications for the recruitment of competent individuals to serve as directors and decision making by them. The report identifies a prohibition on asset rollovers as a provision that might promote integrity in the bankruptcy system, but also notes such potential disadvantages as reduced returns and interference with the reallocation of resources to their most efficient uses. Finally, the possibility of replacement of directors by the Courts was raised.

7. Transfers at Undervalue and Preferences

The IC report questions whether the BIA's current provisions regarding transfers at undervalue and preferences should be modernized and made more comprehensive, since they have remained almost unchanged since the 1919 *Bankruptcy Act* and are generally thought to be unusable. In some cases, the transfers may be fraudulent; in all cases, they occur at the expense of other creditors. Since provincial/territorial legislation governing commercial transactions has been used to address questionable transactions, the report suggests that the fragmentation that currently exists is both confusing and inefficient; a

solution might be the inclusion of provincial/territorial provisions in federal insolvency legislation to form a single, comprehensive regime.

Moreover, the report notes that fraud and intent are difficult to prove, and may involve both costly and lengthy litigation. To resolve this problem, legislation could focus on the result of the transaction, rather than the intent underlying it. This solution is not, however, without problems, particularly for creditors who are more diligent in collecting payments owed to them and for third parties who negotiate a favourable deal immediately prior to a reorganization or insolvency.

8. Bankruptcy by Securities Firms

In 1997, provisions were added to the BIA to enact a regime governing bankruptcies by securities firms. Part of this regime provides a mechanism to override the trust relationship between a securities firm and its customers, and enables almost all securities and cash held by a bankrupt firm to be pooled and distributed *pro rata* among customers, with only "customer name securities" given to customers who own them. The IC report suggests that technical amendments are needed to clarify certain issues that have arisen during recent bankruptcies of securities firms.

9. Application of the *Winding-up and Restructuring Act*

During Industry Canada's consultations with stakeholders, the question of whether the *Winding-up and Restructuring Act* (WURA) should be restricted to financial institutions in situations of insolvency was raised. The IC report notes that, with the availability of the BIA, there is perhaps no reason to allow insolvent companies that are not financial institutions to use the WURA. Moreover, limiting the application of the WURA to financial institutions helps to maintain both the integrity of the system and consistent treatment of companies having a similar purpose.

10. Exemptions for Securities Commissions and Exchanges

Financial regulators – such as securities commissions and exchanges – have expressed concerns about their ability to carry out their regulatory duties in light of reorganization-related stays of proceedings, which have been held to apply to them. The IC report notes broad stakeholder support for the notion that regulatory agencies be exempted from stay provisions. This exemption would enable them to take action against a company that is conducting itself inappropriately, particularly at a time when their control and supervision roles may be most critical.

11. Protection for Trustees against Liability as Successor Employers

The IC report suggests that the standard of liability assumed by a trustee that takes on the role of successor employer should be re-examined. In particular, trustees, receivers and other insolvency administrators who take on this role may be held personally liable for some obligations of a bankrupt or insolvent debtor, including wage, vacation, severance, termination and pension claims, even if the obligations were unknown to them when they accepted the position of trustee, receiver or administrator.

There is some concern that individuals may not be prepared to accept these positions if the risks associated with successor employer obligations are too great. Moreover, they may not be able to assess the risks adequately and quickly when they first accept the positions. The IC report proposes that limits on exposure to liability would encourage individuals to accept such positions, although it would give employees and pensioners fewer options for recourse and would thereby shift the risk from the trustee, receiver or administrator to employees and pensioners.

C. Consumer Insolvency Issues

A range of consumer insolvency issues were identified by stakeholders in the Industry Canada-sponsored consultations, and consensus was reached on a number of concerns, including consumer liens, the growth in consumer bankruptcies, student loans and wage assignments. Significant or extreme differences of opinion, however, existed among stakeholders with respect to: federal exempt property; exemptions for Registered Retirement Savings Plan (RRSPs) and Registered Education Savings Plans (RESPs); reaffirmation agreements; the streamlining of summary administration; the enforcement of security on a bankrupt's household property; and mandatory counselling.

1. Federal Exempt Property and Exemptions for RRSPs and RESPs

At the present time, provinces/territories are responsible for determining the property that is exempt from seizure in bankruptcy; this responsibility, which they have had since 1919, exists with respect to both the nature and the value of the property. Consequently, exempt property varies across Canada. This variability may be of concern, since exemptions play an important role in ensuring that bankrupts receive a fresh start. While some believe that a list of federal exempt property would ensure equitable treatment of bankrupts across Canada, those who support a list of provincial/territorial exempt property suggest that these more accurately reflect local realities and the cost of living.

The IC report notes the suggestion made about an optional list of federal exempt property, periodically adjusted to reflect changes in the cost of living. According to this proposal, bankrupts would be able to select either the list of federal exempt property or the applicable list of provincial/territorial exempt property upon filing for bankruptcy; allowing this choice would not, however, necessarily achieve consistent treatment of exempt property across the country. Other options noted include: a list of federal exempt property as a minimum standard that would apply when provincial/territorial standards were lower; and a list of federal exempt property to replace existing lists of provincial/territorial exempt property. The notion of monetary limits – whether in a list of federal or provincial/territorial exempt property – received support during Industry Canada's consultations.

Regarding Registered Retirement Savings Plans, the IC report notes that certain retirement savings vehicles – including registered pension plans, locked-in RRSPs and life insurance RRSPs – are exempt from seizure in bankruptcy. Other vehicles – including non-locked-in RRSPs held by banks, brokerages or in self-directed accounts – are not, however, exempt. Stakeholders have suggested that, for reasons of equity, all retirement savings vehicles should be treated in the same manner; from this perspective, non-insurance RRSPs should be exempt from seizure in bankruptcy if they are locked in.

The IC report identifies arguments against this treatment of non-insurance RRSPs: it would reduce returns to creditors; RRSPs can be used for reasons unrelated to retirement; and RRSP holders currently have the option of protecting their RRSPs through the purchase of life insurance RRSPs. Nevertheless, a specified number of options for change are identified in the report: exempt RRSPs provided they are locked in and only available at retirement; ensure that contributions made by the debtor in a specified number of years before bankruptcy would not be exempt from seizure; stipulate that income from an RRSP payable following retirement would be treated as income and subject to surplus income standards; impose a cap on the exemption, bearing in mind the bankrupt's age and the maximum RRSP contribution limit available in the year of bankruptcy; and no exemption for RRSPs, since they are identical to other investments.

A final exemption raised in the IC report's examination of consumer insolvency issues is the treatment of Registered Education Savings Plans. In particular, the report questions whether amounts contributed to an RESP should be exempt from seizure if the person in whose name the account is held becomes bankrupt. At the present time, bankruptcy by the plan holder results in the existing balance being seized to pay creditors and in the contributions made by the federal government being returned to the government.

The main issue regarding RESPs appears to be the balance between the fairness of exempting another asset from seizure in bankruptcy, and thereby reducing the returns to creditors, and the promotion of education in the public interest. The IC report also notes the concern that additional exemptions and prioritizing of claims reduce the fundamental premise on which Canadian insolvency law has been drafted: the fair and efficient redistribution of assets. The parallel between RESPs and RRSPs – and the public interest in both – was identified. Stakeholders have suggested options similar to the proposals for RRSPs, including: locking-in requirements and a clawback of contributions made in the

previous year. Another proposal was for RESPs to meet the formal requirements of a trust, which would make the funds exempt from seizure, although the flexibility of the plans would be reduced.

2. Reaffirmation Agreements

The IC report identifies concerns by stakeholders about whether reaffirmation agreements, which re-establish a debt that has been discharged by bankruptcy, should be legal; at present, such agreements are not regulated by the BIA. Some stakeholders believe that the existence of these agreements undermines the fresh start principle, although it may be the only means by which a bankrupt can obtain credit.

One proposal noted in the report would disallow reaffirmation agreements concerning unsecured transactions, but would allow some payments under two circumstances: if approved by the Official Receiver or the Court or made voluntarily to a relative, and in respect of secured transactions in limited circumstances. Another proposal identified in the report is a prohibition on reaffirmation agreements in all circumstances, which would support the fresh start principle but perhaps affect the availability and cost of credit; it would also prohibit such agreements even in situations where reaffirmation might be in the best interest of both parties.

3. Summary Administration

For debtors with limited assets and a modest income, simplified procedures for consumer bankruptcies might be desirable. Historically, Canadian insolvency legislation was designed to resolve bankruptcies by companies, and a streamlined process for debtors with limited assets was not available until 1949 when summary administration provisions were added to the *Bankruptcy Act*. At present, these provisions apply to non-corporate bankruptcies with realizable assets no greater than $10,000. The IC report notes that the process, nevertheless, is still relatively complex; moreover, with consumer bankruptcies rising – particularly among debtors with few or no assets and low income – it would be efficient to process these cases as quickly and inexpensively as possible.

Options for reform suggested by stakeholders include: modifying the process to eliminate procedures that add no value; allowing creditors, the Office of the Superintendent of Bankruptcy and trustees to get involved in bankruptcies selectively; and performing select administrative tasks only if requested by creditors. With such changes, however, there would be a need to ensure that the integrity of the system is protected and abuse is prevented; one means for achieving these goals might be to delay discharge for up to three years.

4. Household Property

The IC report questions whether the current provision allowing the enforceability of security agreements on a debtor's household property following bankruptcy should be changed. In most provinces/territories, creditors can take, as security, the personal property found in a debtor's home. There is a concern that, in the event of bankruptcy or insolvency, creditors could take advantage of the debtor's desire to keep this property by demanding – and obtaining through the threat of seizure – more than the property is worth.

Some stakeholders believe that the provisions allowing this practice result in bankrupt individuals and their families being abused. One proposal identified in the report would make all non-purchase money security interests granted by the debtor against exempt personal property unenforceable in bankruptcy and proposals; it would also enhance protection for assets that are exempt from seizure and require a secured creditor to pay the exempt amount to the debtor prior to enforcement. A suggestion has also been made that motor vehicles might be treated differently than other household belongings. Limitations on security interests in household furnishings could, however, affect the availability of credit for the purchase of these assets.

5. Mandatory Counselling

Since amendments to the BIA in 1992, mandatory counselling has been required for first-time bankrupts before receiving an automatic discharge from bankruptcy; counselling is also required for debtors making consumer proposals. The IC report suggests that counselling is beneficial in a number of ways and appears to have had only a limited impact on operating costs, with the result that creditors are not being unduly disadvantaged by the fact that counselling is financed by the bankrupt's estate.

Nevertheless, some believe that counselling should be optional and at the discretion of the debtor, the trustee or the Office of the Superintendent of Bankruptcy. Others have suggested more counselling, earlier counselling and counselling as a requirement in all cases. The notion of a comprehensive education program on personal finance for youth was also identified in the report.

Those who are opposed to mandatory counselling have argued that it occurs too late in the process, with the result that it is not effective, and that bankruptcy is often the result not of financial mismanagement but instead of such situations as business failure, job loss or change in marital status.

6. Consumer Liens

At present, consumers who place deposits with vendors for goods or services, but who do not receive those goods or services as a consequence of bankruptcy by vendors, are unprotected by the law. As unsecured claims, these consumers have few opportunities for recovery; in the majority of cases, they do not view themselves as creditors and did not intend to incur any risk.

The IC report notes that a consumer lien would increase the likelihood of recovery for these consumers, although it would give statutory protection to a specific group of creditors at the expense of other creditors and might affect the availability of credit. The report also presents the relatively weaker option of giving such consumers preferred status, behind secured creditors but ahead of claims by ordinary creditors; any negative effects on credit availability would likely be smaller with this option. Alternatively, this issue could be resolved through provincial/territorial commercial/consumer legislation, although constitutional issues might be raised where a provincial/territorial law of this nature purports to be applicable in a bankruptcy.

7. Student Loans

Amendments to the BIA in 1998 provide that any outstanding student debt and interest owing on those debts will not be discharged by bankruptcy should the debtor become bankrupt while a student or within ten years after completing his or her studies; prior to this change, the restriction was two years after the completion of studies. The amendment occurred as a consequence of the 1998 federal Budget, which made several changes to the federal student assistance program and provided students with an incentive to take advantage of relief measures as an alternative to bankruptcy.

The IC report questions whether this ten-year restriction on the ability of bankrupt students to obtain a discharge should be modified. Stakeholders believe that the restriction is too harsh and unfair, and that student loans should be treated in the same manner as other consumer debt. Options for change include reducing the ten-year period to five years and/or making student loan debt a preferred claim but still discharged by the bankruptcy.

8. Wage Assignments

Wage assignments, which are permitted in some provinces, are a form of security for consumer loan granted by credit unions in which the collateral is a portion of the future wages of the debtor. With amendments to the BIA in 1992, assignments of future or existing wages made before bankruptcy do not apply to post-bankruptcy wages, with the result that other creditors are receiving moneys that previously were received by the credit

unions; prior to the change, wage assignments were enforceable against wages earned after bankruptcy but before discharge.

The IC report notes that some stakeholders would like the effectiveness of wage assignments to be restored; this view is held particularly by those in the financial community. It suggests, however, that the fresh start principle may be undermined if the collateral in a wage assignment consists of a substantial portion of the debtor's future earnings, and that the availability of wage assignments reduces the amounts available to other creditors since surplus income would likely fall. Nevertheless, such assignments may be the only collateral available to the debtor. As well, since wage assignments reduce the risk for credit unions, the availability and cost of credit may be positively affected.

APPENDIX D:
AN INTERNATIONAL PERSPECTIVE ON INSOLVENCY LAW

A. The United States

In the United States, the *Bankruptcy Reform Act* of 1978 – commonly referred to as the *Bankruptcy Code* – is the major bankruptcy statute. Since it became effective in November 1979, it has been amended a number of times, including by the *Bankruptcy Amendments and Federal Judgeship Act* of 1984, the *Bankruptcy Judges, United States Trustees, and Family Farmer Bankruptcy Act* of 1986 and the *Bankruptcy Reform Act* of 1994. Chapter 11 of the *Bankruptcy Code* is the major insolvency procedure, and is often used in preference to Chapter 7. Chapter 11 involves reorganization, while Chapter 7 involves liquidation and is used mostly by those wishing to free themselves of debt; as well, Chapters 12 and 13 involve reorganization.

A voluntary petition for bankruptcy can occur under Chapters 7, 11, 12 or 13, although involuntary petitions – which involve a petition by creditors – are limited to Chapters 7 and 11. Most Chapter 11 actions involve corporate debtors and are voluntary; insolvency is not required for a Chapter 11 filing to be initiated. Reorganizations can also occur under Chapter 12 – which applies to farmers – and Chapter 13 – which is typically used by consumer debtors with regular income. While insolvent consumers can file under Chapter 7 only once every six years, there is no limit on the number of times they can file under Chapter 13, provided the pre-established percentages of debt have been repaid.

Unlike a number of other developed countries, except Canada, during reorganizations under Chapter 11 the company usually retains control and management functions, subject to certain restrictions. The Court must approve any disposals outside of the normal course of business, and provision is made for the appointment of a trustee and/or an examiner by the Court, although it rarely occurs. Proceedings under Chapters 12 and 13 typically involve the appointment of a trustee to supervise the debtor's assets, although the debtor retains control of them.

Under reorganization, the debtor – whether a consumer or a corporation – is required to present any debt reorganization proposal to class meetings of creditors, and those whose rights have been impaired by the proposal are permitted to vote. As well, the proposal must be approved by the Court, which considers fairness criteria and must be satisfied both that the proposal is feasible and that dissenting creditors will receive at least as much under the proposal as they would if the company were liquidated. The Court may disregard a creditors' vote rejecting the proposal, and instead confirm it if it determines that creditors

would be treated fairly. In Chapter 13 filings, the maximum period of debt adjustment is five years.

Chapter 7 proceedings – which can be initiated voluntarily or by creditors – require the appointment of a trustee who seizes the non-exempt property of the debtor, liquidates the assets and distributes the proceeds to creditors; the *Bankruptcy Code* establishes the priority of creditors' interests.

As well, the *Bankruptcy Code* contains federal exemptions, although individual states are free to establish their own exemptions and can preclude their residents from using the federal exemptions. If their state of residence has not established its own exemptions and has not precluded its residents from using the federal exemptions, the bankrupt can choose to apply either the state or the federal exemptions.

In particular, the federal exemptions include:

- a homestead consisting of real property, to a maximum value;
- alimony and child support payments;
- pension and retirement benefits;
- household goods and furnishings, to a maximum value;
- health aids;
- jewellery, to a maximum value;
- lost earnings payments;
- a motor vehicle, to a maximum value;
- personal injury compensation payments, to a maximum value;
- wrongful death and crime victims' compensation payments;
- public assistance, social security, unemployment compensation and veterans' benefits;
- trade tools, to a maximum value;
- property, to a maximum value; and
- other exemptions related to insurance policies.

Exemptions vary relatively widely from state to state, which means that debtors are subject to significantly different treatment depending on their state of residence.

A bankruptcy proceeding ends when the Bankruptcy Court enters a discharge order regarding dischargeable debts. This action generally occurs no later than six months after the debtor files the bankruptcy petition, and coincides with the expiration of the time fixed for filing a complaint objecting to discharge and the time fixed for filing a motion to dismiss the case for substantial abuse. A complaint may be filed by a creditor, the trustee or the

United States trustee; the filing begins a lawsuit, referred to as an "adversary proceeding," in which the objecting party bears the burden of proof. A discharge can be revoked under certain circumstances. The bankruptcy remains on the debtor's credit record for up to ten years. Finally, a discharged debtor may voluntarily repay any debt that has been discharged.

At present, comprehensive bankruptcy reform legislation is before Congress. Proposed Chapter 15 of the legislation would enact, insofar as possible, the UNCITRAL Model Law on Cross-Border Insolvency. As currently drafted, proposed Chapter 15, like the Model Law itself, contains no reciprocity requirement.

B. The United Kingdom

In the United Kingdom, insolvent debtors have a number of options available to them, including: administration orders; individual voluntary arrangements; and bankruptcy. An administration order may occur where a creditor(s) obtains a Court judgment against a debtor who has no more than £5,000 in debt. Administration is a Court-based procedure whereby the debtor makes regular payments to the Court for payment to creditors.

With an individual voluntary arrangement, the debtor makes a formal proposal to creditors to pay his or her debts in whole or in part. The debtor applies to the Court for an interim order and selects an authorized insolvency practitioner; the practitioner presents the Court with the details of the proposal and an indication of whether a meeting of creditors should be convened to consider the proposal. If more than 75% in value of the creditors who vote are in favour of the proposal, then the proposal is accepted and is binding on all creditors who are entitled to vote. The insolvency practitioner then supervises the arrangement and pays the creditors in accordance with the proposal.

The Court will make a bankruptcy order after a bankruptcy petition has been presented by the debtor or by one or more unsecured creditors who are owed £750. An Official Receiver – who is an officer of the Court – is responsible for administering the bankrupt's estate and acts as trustee unless an insolvency practitioner is appointed; as a consequence, he or she examines the bankrupt's financial affairs prior to and during the bankruptcy, and reports to the Court and to creditors.

With certain exceptions, the Official Receiver/Trustee controls the bankrupt's assets – subject to exemptions – and disposes of them, with the proceeds used to pay the fees, costs and expenses of the bankruptcy as well as creditors. There are two broad categories of exemptions: one for the property required to earn a living, the other for household possessions needed to meet basic needs. In particular, the exemptions – which contain no limits on value, but rather allow the trustee to determine the value based on individual and family situation – are:

- tools, books, vehicles and other equipment needed for the bankrupt's personal use in employment, business or vocation; and

- clothing, bedding, furniture, household equipment and provisions needed to satisfy basic domestic needs of the bankrupt and his or her family.

Moreover, the trustee generally cannot claim a pension as an asset if the bankruptcy petition was presented on or after 29 May 2000, provided the pension scheme has been approved by the Inland Revenue; trustees can claim some kinds of pensions for petitions presented before that date. The trustee can usually claim any interest the bankrupt has in a life assurance policy. Moreover, the trustee may apply to the Court for an income payments order which would require the bankrupt to make contributions to the bankruptcy debt from his or her income until the discharge from bankruptcy; such an order would not be made if it would leave the debtor without sufficient income to meet his or her reasonable domestic needs and those of his or her family.

At present, discharge from bankruptcy generally occurs automatically after three years, although if the bankruptcy order refers to a certification of summary administration – where a bankrupt has filed his or her own petition and the unsecured debts are less than £20,000 – the discharge occurs after two years; if the order is cancelled, discharge is automatic. These provisions will change as a consequence of the *Enterprise Act 2002*, as indicated below. Nevertheless, if the bankrupt has not fulfilled his or her duties under the bankruptcy proceedings, the Official Receiver may apply to the Court for the discharge to be postponed. As well, discharge is currently not automatic if the bankrupt has been an undischarged bankrupt at any time during the previous 15 years; however, the bankrupt may apply to the Court for discharge any time after five years from the date of the current bankruptcy order, and the Court may refuse or delay the discharge or grant it conditionally. The *Enterprise Act 2002* will also change this provision.

In the United Kingdom, companies in financial distress have a number of options: administration; Company Voluntary Arrangements; receivership; liquidation; and dissolution. Since 1985, there have been two forms of rescue procedure for organizations. An administration order – a Court order – can be made by petition of the company's directors, the company itself or creditors. It must be demonstrated that the company is – or is nearly – insolvent, and that one or more of four purposes would be served by the order, one of which is related to the Company Voluntary Arrangement procedure introduced in 1985; the other three are: survival of the company as a going concern; a Court-sanctioned composition or arrangement; or there is likely to be a better realization of assets than would be the case with a liquidation.

The Company Voluntary Arrangement was conceived as a compromise procedure whereby a debtor company could make a proposal to creditors, and an independent insolvency practitioner would report to the Court on the viability of the proposal. The Court has the discretion whether to make an administration order.

Finally, the *Enterprise Act 2002* – designed to enhance enterprise and productivity – made relatively significant changes to insolvency law in parts of the United Kingdom. The changes related to individual insolvency will come into force on 1 April 2004, while corporate insolvency changes have been in effect since 15 September 2003. While most of

the provisions will apply throughout the United Kingdom, the bankruptcy reforms related to discharge will apply in England and Wales only, and the corporate insolvency reforms do not apply in Northern Ireland.

One area of change is automatic discharge from bankruptcy; people made bankrupt on or after 1 April 2004 will receive an automatic discharge after one year, rather than the current two- or three-year period. Moreover, for those who have been an undischarged bankrupt at any time in the previous 15 years, a discharge will occur at the earlier of: 1 April 2009 or a date ordered by the Court; bankrupts may apply to the Court for discharge five years after the date of their present bankruptcy order and if this date is before 1 April 2009, they may apply to the Court to be discharged then. Regarding corporate insolvency, the *Enterprise Act 2002* abolishes the Crown's preferential right to recover certain unpaid taxes ahead of other creditors and provides that unsecured creditors will share in essentially 20% of the proceeds of the liquidation of debenture security (inventory and accounts receivable), to a maximum of £600,000.

C. Australia

In Australia, the *Bankruptcy Act 1966* addresses personal bankruptcy and alternative arrangements with creditors, while the *Corporations Law* deals with corporate insolvencies. Although this latter statute is uniform across the country, for constitutional reasons state and territorial statutes have been enacted.

Options available to insolvent consumers who are unable to pay their debts as they are due to be paid include:

- under Parts IX and X of the *Bankruptcy Act*, debtors can enter into arrangements with creditors that may involve payment of less than the full amount of debt, a moratorium on payments of debt, transfers of property to one or more creditors in full or partial payment of debt, or periodic payments to creditors out of the debtor's income; or
- debtors can have their estate administered in bankruptcy, whether the bankruptcy occurs voluntarily or – more rarely – involuntarily pursuant to a creditor's petition.

A Part IX debt agreement requires that the debtor:

- not have been bankrupt, used a debt agreement or given an authority under Part X of the *Bankruptcy Act* in the previous ten years;
- have after-tax income of less than approximately A$50,000;
- have unsecured debts of less than approximately A$67,000; and

- have property not exempt under bankruptcy valued at less than approximately A$67,000.

Options available under Part X arrangements include:

- a deed of assignment, pursuant to which a debtor assigns all divisible property for the benefit of creditors;
- a composition, pursuit to which creditors accept repayment over time or partial payment in full satisfaction; or
- a deed of arrangement, pursuant to which the debtor repays debts, either in whole or in part, but in a manner that does not fall within the definition of either a composition or a deed of assignment.

In most situations, after-acquired property is unaffected and the debtor is under no obligation to make contributions from income to creditors.

To avoid bankruptcy, a debtor may enter into alternative arrangements with his or her creditors and may present a proposal at a meeting of creditors. To conclude an arrangement that is binding on all creditors with provable debts, the proposal must be approved by a majority in number and at least 75% in value of the creditors who vote at the meeting.

Low-income debtors with limited – if any – property, few creditors, low viability and financial resources too low to enable them to take advantage of a deed of assignment, a deed of arrangement or a composition because of an inability to meet set up costs, can enter into a debt agreement provided they meet asset, liability and after-tax income stipulations. With this procedure, the debtor submits a proposal and a Statement of Affairs to the Official Trustee. After determining that the debtor meets the eligibility requirements for this process, the Official Trustee advises creditors of the proposal, provides them with a summary of the debtor's Statement of Affairs and allows the creditors to vote on the proposal. The degree of acceptance required for the debt agreement to be binding is a majority in number and at least 75% in value of the creditors who vote on the proposal.

A debtor who voluntarily seeks bankruptcy presents a debtor's petition to an Official Receiver together with a Statement of Affairs providing his or her personal details as well as details of his or her assets, liabilities and income. The debtor becomes a bankrupt when the petition is accepted, and the Official Receiver becomes the trustee, unless the debtor nominates a private registered trustee.

Involuntary bankruptcy involves the presentation of a creditor's petition in the Federal Court or the Federal Magistrates Court. This action requires that the following circumstances be met: an act of bankruptcy within the previous six months; a specific jurisdictional link with Australia; and a liquidated sum of A$2,000 owed by the debtor to the creditor. At the hearing of the petition, the creditor is required to prove: the matters stated in the petition; the service of the petition; and the outstanding nature of the debt owed. The

Court has discretion in deciding whether to make a sequestration order, which is an order making a person or persons bankrupt.

A bankrupt receives automatic discharge from bankruptcy three years after the date on which the Statement of Affairs is filed, unless an objection is lodged; for example, a trustee's objection may prolong bankruptcy by as much as five years under certain circumstances. The bankrupt may be able to apply for an early discharge six months after the filing date, although this provision applies only to bankruptcies registered with the Official Receiver prior to 5 May 2003. Bankrupts with relatively high incomes must make contributions to their bankrupt estates from their income, with the amount determined on the basis of net income after tax and any child support. Creditors are prohibited from recovering money from a bankrupt, other than secured creditors with whom the bankrupt has made an arrangement to retain secured property, such as might occur with a mortgage.

Australia makes provision for exempt property in the case of bankruptcy, and these exemptions are uniform throughout the country; Australia does not have inter-state differences with respect to exemptions, either in type or value. Principal exemptions include:

- property held by the bankrupt in trust for another person;
- the bankrupt's household property, to reasonable limits given current social standards or that is exempted under regulations or by agreement of the creditors;
- property used by the bankrupt in earning income, to a prescribed limit or as increased by creditors or the Court;
- property used by the bankrupt primarily for transportation, to a prescribed limit or as approved by creditors;
- prescribed interests in life or endowment assurance and in regulated superannuation funds or approved deposit funds;
- compensation for personal injuries and property purchases with such protected money; and
- amounts paid to the bankrupt as loan assistance for rehabilitation, household or re-establishment support under a variety of state and federal rural support schemes.

Insolvent companies have a number of options: a Court-sanctioned arrangement; appointment of a receiver or other controller; voluntary administration; winding-up/liquidation; or provisional liquidation. Since mid-1993, Australia has had a voluntary administration procedure by which a company or its directors can initiate the procedure, and secured creditors with charges over all – or substantially all – of the assets may initiate the appointment of an administrator. Once appointed, the administrator controls the company's business, its property and its affairs, and acts as the company's agent. He or she must hold a meeting of creditors, and creditors will meet to decide the company's future; the

creditors will receive a report about the business and its property, affairs and financial circumstances, as well as an assessment of whether it would be in the creditors' interests for the company to execute a deed of company arrangement, for the company to be wound up or for the administration to end.

In September 2002, the Attorney General of Australia announced that the government would conduct a comprehensive review of Part X of the *Bankruptcy Act 1966*, which provides a mechanism for debtors to reach arrangements with creditors without becoming bankrupt. The review was initiated in response to concerns that some debtors are abusing the provisions. Conducted by the Insolvency and Trustee Service Australia (ITSA) – which is responsible for the administration and regulation of the personal insolvency system – and the Attorney General's Department, in consultation with the Bankruptcy Reform Consultative Forum, the ITSA released an issues paper describing proposed legislative changes for public comment.

The Bankruptcy Legislation Amendment Act Bill 2002 was introduced in order to address concerns that the system was biased toward the debtor, to correct unfairness and anomalies, and to streamline the administration of bankruptcies by trustees. In particular, the Bill was designed to:

- give Official Receivers the discretion to reject a petition made by a debtor where it appears that, within a reasonable period of time, the debtor could pay all debts listed in his or her Statement of Affairs and that the petition is an abuse of the system, or where the debtor has been bankrupt previously – on his or her own petition – either at least three times in all or at least once in the previous five years;
- abolish early discharge from bankruptcy;
- make it easier for trustees to lodge objections to a person's discharge from bankruptcy and make it harder for bankrupts to sustain challenges to objections;
- make clear that a bankruptcy can be annulled by the Court whether or not the bankrupt was insolvent when the petition for bankruptcy was accepted; and
- increase the income threshold for debt agreements.

Amendments to the *Bankruptcy Act 1966* and regulations came into effect on 5 May 2003, and increased the debt agreement threshold to more than a A$50,000 (after taxes), thereby increasing the number of debtors eligible to participate in debt agreements.

D. New Zealand

In New Zealand, bankruptcy and insolvency are addressed primarily through the *Insolvency Act 1967* (personal insolvency), the *Companies Act 1993* (corporate liquidations) and the

Receiverships Act 1993 (corporate receiverships). The *Corporations (Investigations and Management) Act 1989* may be used in situations where the government wishes to place a complex group of companies into statutory management. The New Zealand Insolvency and Trustee Service – through the office of Official Assignee (Ministry of Commerce) – is the only agency with authority to administer personal bankruptcies, and the High Court has jurisdiction over all insolvency matters.

New Zealand insolvency law provides a number of options to individuals in financial difficulty, including:

- a creditors' pool, where all of the debtor's creditors agree to receive payment in reduction of debt through regular instalments;
- a compromise with creditors, where an agreement is reached regarding payment of a portion of debt in full settlement;
- a Summary Instalment Order, which involves an order by a District Court Judge that allows a person with debts less than a certain amount to pay those debts in regular instalments without further legal action being taken while the order is in force; and
- bankruptcy, which can be initiated either by the debtor or by the creditor.

A debtor who selects bankruptcy as the preferred option files a Debtor's Petition with the High Court; alternatively, bankruptcy can be initiated by the creditor applying to the High Court, which then must decide if the debtor should be declared bankrupt on the basis of evidence supplied by the creditor and the debtor (or his or her representative). The Official Assignee, an officer of the High Court, is trustee and must administer equitably and independently the affairs of the bankrupt, with the non-exempt assets sold and the proceeds distributed fairly among the creditors; he or she may also provide for rehabilitation of the bankrupt, if appropriate.

Exempt assets include furniture and personal effects, money, and tools of a tradesperson's trade, up to a maximum amount in each case. The Official Assignee will decide whether the debtor will retain his or her vehicle, with that decision based on the vehicle's value and the debtor's personal circumstances. As well, life insurance policies become the property of the Official Assignee and may be surrendered for the benefit of creditors, and superannuation policies with a surrender value may also be included. Bankrupts remain responsible for a number of debts, including Court-imposed fines, maintenance payments and child support obligations.

In general, the bankrupt will receive an automatic discharge on the third anniversary of his or her bankruptcy, although an application may be made to the High Court for an earlier discharge. The Official Assignee or a creditor may, however, object to a discharge or seek a conditional discharge; in the event of an objection to an automatic discharge, the High Court will decide the date of discharge. Finally, bankrupts may apply for an annulment of bankruptcy, which would involve the High Court cancelling the bankruptcy order; this

situation may occur if: the bankruptcy order should not have been made; all of the debtor's debts, fees and expenses of bankruptcy have been paid in full; or creditors accept a composition.

In terms of corporate bankruptcy, there are several means by which a company may be put into liquidation: by a special resolution of the organization's shareholders; by the company's board of directors when an event specified in the constitution has occurred; or by the Court, on application of the company, a director, a shareholder or a creditor. A liquidator is appointed who then has custody and control of the organization's assets. A report indicating the company's assets and liabilities is prepared and provided to creditors, and the assets are sold for the benefit of those creditors who have lodged a claim in the liquidation. A dividend is paid to creditors in the order of priority given in the *Companies Act 1993*.

In May 1999, New Zealand launched a review of insolvency law in order to:

- provide a predictable, simple regime that: can be administered quickly and efficiently; imposes the minimum necessary compliance and regulatory costs on users; and does not stifle innovation, responsible risk taking and entrepreneurship by excessively penalizing business failure;
- distribute the proceeds to creditors consistent with their relative pre-insolvency entitlements, unless the public interest requires otherwise;
- maximize returns to creditors;
- enable bankrupt individuals again to participate fully in the economic life of the community; and
- provide international cooperation in relation to cross-border insolvency.

Public discussion documents were released beginning in February 2001, and since that time the Ministry of Economic Development has indicated that the law will be changed in a number of areas. In particular, the following initiatives have been announced:

- continued responsibility by the state for bankruptcy administration;
- a business rehabilitation system, which will resemble that which operates in Australia and will provide an alternative to liquidation through which a debtor organization or individual can reach a binding arrangement with creditors;
- as an alternative to bankruptcy, a "no asset" procedure for low-income debtors with limited – if any – realizable assets;
- criminal penalties to be imposed on directors who have acted in bad faith to defeat creditors' legitimate interests;
- increases in the maximum amount to which employees will be entitled – for unpaid wages, salary and vacation pay – in the event of insolvency by their

employer and the introduction of redundancy payments as an employee entitlement;

- an increase in the cap for Summary Instalment Orders; and
- adoption of the UNCITRAL Model Law on Cross-Border Insolvency.

It is anticipated that, following public consultation on draft legislation, the changes will become law no later than 2004.

APPENDIX E:

Witnesses and Submissions:

Advocis
- Mr. Steve Howard, CA, President and Chief Executive Officer (Wednesday, May 14, 2003)
- Mr. Edward Rothberg, General Counsel (Wednesday, May 14, 2003)

Alberta Law Reform Institute
- Professor C. R. B. (Dick) Dunlop, Special Counsel (Thursday, September 18, 2003)
- Mr. Peter J. M. Lown, Director (Thursday, September 18, 2003)

Mr. Ryan Bailey
- Manager - Government Relations and Regulatory Affairs, Ontario Society of Professional Engineers (Submission)

Mr. David E. Baird, Q.C.
- Counsel, Torys LLP (Thursday, September 25, 2003)

Professor Douglas Barbour
- Department of English, University of Alberta (Submission)

Me Hélène Beaulieau
- Barrister and Solicitor (Submission)

Professor Vaughan Black
- Professor of Law, Dalhousie University (Submission)

Canadian Association of Insolvency and Restructuring Professionals
- Mr. Larry Prentice, Chair CAIRP, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professionals) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)
- Mr. Jean-Yves Fortin, President, IIC, Lawyer (Thursday, May 8, 2003)
- Mr. Andy Kent, IIC Board member, Lawyer (Thursday, May 8, 2003)
- Mr. William Courage, Vice-Chair CAIRP, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professionals) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)
- Mr. Alan Spergel, Co-Chair CAIRP – Personal Insolvency Practice Committee, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professional) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)

Canadian Association of Insolvency and Restructuring Professionals (Cont'd)

- Mr. Stéphane LeBlond, Vice-Chair CAIRP – Personal Insolvency Practice Committee, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professional) and CA (Thursday, May 8, 2003)
- Mr. George Lomas, member of IIC Personal Insolvency Committee, Trustee in bankruptcy, FCA, FCIRP (Chartered Insolvency and Restructuring Professional) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)

Canadian Alliance of Students Associations

- Mr. Rob South, Government Relations Officer (Wednesday, May 14, 2003)

Canadian Bankers Association

- (Submission)

Canadian Bar Association

- Mr. David F. W. Cohen, Chair, National Bankruptcy and Insolvency Law Section (Wednesday, June 4, 2003)
- Mr. Robert A. Klotz, Executive Member and Past Chair, National Bankruptcy and Insolvency Law Section (Wednesday, June 4, 2003)
- Mr. E. Patrick Shea, Member, National Bankruptcy and Insolvency Law Section (Wednesday, June 4, 2003)
- Mrs. Tamra L. Thomson, Director, Legislation and Law Reform, Canadian Bar Association (Wednesday, June 4, 2003)

Canadian Federation of Independent Business

- Mr. Garth Whyte, Executive Vice President (Wednesday, October 1, 2003)
- Mr. André Piché, Director, National Affairs (Wednesday, October 1, 2003)

Canadian Federation of Students

- Mr. Michael Conlon, Director of Research (Wednesday, May 14, 2003)

Canadian Labour Congress

- Mr. Hassan Yussuff, Secretary-Treasurer (Wednesday, September 17, 2003)
- Mr. Bob Baldwin, Director, Social and Economic Policy (Wednesday, September 17, 2003)
- Mr. Murray Gold, Partner, Koskie Minsky (Wednesday, September 17, 2003)

CAW-Canada

- Mr. Lewis Gottheil, Counsel (Wednesday, September 17, 2003)

Consumers Association of Canada

- Mr. Mel Fruitman, President and Chief Executive Officer (Wednesday, September 17, 2003)

Consumers' Union

- Mrs. Hélène Talbot, Budget Counsellor, Canadian Tax Foundation (Wednesday, May 14, 2003)
- Mr. Luc Rochefort, Analyst, Policy and Legislation in Personal Budgeting, Credit and Debts (Wednesday, May 14, 2003)

Credit Counselling of Canada
- Mr. Pran Bahl, President (Wednesday, September 17, 2003)
- Mr. Pierre R. Ouellette, Executive Director (Wednesday, September 17, 2003)

Credit Union Central of British Columbia
- (Submission)

Professor R.C.C. Cuming
- Professor of Law, University of Saskatchewan (Submission)

Mr. Jean-Claude Delorme
- Chairman of the Management Advisory Board of the Office of the Superintendent of Bankruptcy (Thursday, September 25, 2003)

Ms. Viola Doucet
- (Wednesday, May 14, 2003)

Professor Elizabeth Edinger
- Associate Dean of Law, University of British Columbia (Submission)

Equifax Canada Inc.
- Mr. Mel Zwaig, President & Chief Executive Officer, Zwaig Consulting Inc. (Wednesday, October 1, 2003)
- Mr. E. Bruce Leonard, Cassels Brock & Blackwell LLP (Wednesday, October 1, 2003)
- Mr. David S. Ward, Cassels Brock & Blackwell LLP (Wednesday, October 1, 2003)

Mrs. Lori K. Gravestock
- Submission

Human Resources Development Canada
- Mr. Andrew Treusch, Assistant Deputy Minister, Human Investment Programs (Wednesday, October 1, 2003)
- Mr. Dave Cogliati, Director General, Canada Student Loans Program Directorate (Wednesday, October 1, 2003)

Industry Canada
- Marie-Josée Thivierge, Director General, Marketplace Framework Policy Branch (Wednesday, May 7, 2003)
- Marc Mayrand, Superintendent of Bankruptcy, Office of the Superintendent of Bankruptcy (Wednesday, May 7, 2003)
- Jim Buchanan, Senior Project Leader, Policy Sector (Wednesday, May 7, 2003)
- Dave Stewart, Senior Project Leader, Office of the Superintendent of Bankruptcy (Wednesday, May 7, 2003)

Insolvency Institute of Canada
- Mr. Larry Prentice, Chair CAIRP, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professionals) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)

Insolvency Institute of Canada (Cont'd)

- Mr. Jean-Yves Fortin, President, IIC, Lawyer (Thursday, May 8, 2003)
- Mr. Andy Kent, IIC Board member, Lawyer (Thursday, May 8, 2003)
- Mr. William Courage, Vice-Chair CAIRP, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professionals) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)
- Mr. Alan Spergel, Co-Chair CAIRP – Personal Insolvency Practice Committee, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professional) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)
- Mr. Stéphane LeBlond, Vice-Chair CAIRP – Personal Insolvency Practice Committee, Trustee in bankruptcy, CIRP (Chartered Insolvency and Restructuring Professional) and CA (Thursday, May 8, 2003)
- Mr. George Lomas, member of IIC Personal Insolvency Committee, Trustee in bankruptcy, FCA, FCIRP (Chartered Insolvency and Restructuring Professional) and CA-CIRP (CA specialist in insolvency and restructuring) (Thursday, May 8, 2003)

Intellectual Property Institute of Canada

- Mr. John Baker, Immediate Past President (Wednesday, September 24, 2003)
- Mr. Warren Sprigings, Chairman of the Licensing Committee (Wednesday, September 24, 2003)
- Mr. Rodney Kyle, Member of the Licensing Committee (Wednesday, September 24, 2003)
- Mr. Michel Gérin, General Director (Wednesday, September 24, 2003)

International Insolvency Institute

- E. Bruce Leonard, Chairman (Wednesday, June 4, 2003)

Mr. Andrew J.F. Kent

- McMillan Binch LLP (Submission)

Mr. Robert A. Klotz

- Executive Member and Past Chair, National Bankruptcy and Insolvency Law Section, Canadian Bar Association (Wednesday, June 4, 2003) (Submission)

Mr. Bert van Leeuwen

- President, BVL Industrial Design Ltd. (Submission)

Mr. Bob van Leeuwen

- President, van Leeuwen Engineering Limited (Wednesday, June 4, 2003)

Mr. E. Bruce Leonard

- Chairman, International Insolvency Institute; Cassels Brock & Blackwell LLP (Wednesday, June 4, 2003 & Wednesday, October 1, 2003) (Submission)

Mrs. Nancy May

- (Submission)

Mr. Max Mendelsohn

- Chairman of the Firm and Head of the Reorganizations & Insolvency Group of Mendelsohn, G.P. (Thursday, September 25, 2003)

Mr. Brian P. O'Leary
- Burnet, Duckworth & Palmer LLP (Submission)

Omega One Ltd.
- Mr. Bob Gilmour, Manager, Asset Recovery, Sears Canada Inc. (Wednesday, May 14, 2003)
- Mr. John D. Owen, Principal (Wednesday, May 14, 2003)

Ontario Securities Commission
- (Submission)

Periodical Writers Association of Canada
- (Submission)

Personal Insolvency Task Force
- Mr. Saul Schwartz, School of Public Policy and Administration, Carleton University (Wednesday, September 24, 2003)
- Mr. Dave Stewart, Special Project Leader, Office of the Superintendent of Bankruptcy (Wednesday, September 24, 2003)
- Mrs. Guylaine Houle, Litwin Boyadjian Inc. (Wednesday, September 24, 2003)

Mr. Michael Petrasek
- Rights Manager, Playwrights Guild of Canada (Submission)

A.C. Poirier & Associates
- Mr. Paul A. Stehelin, Trustee in Bankruptcy (Wednesday, May 14, 2003)

Professor Iain D.C. Ramsay
- Professor of Law, Osgoode Hall Law School (Submission)

RESP Dealers Association of Canada
- Mrs. Doreen G. Johnston, Chairman, Securities Regulation (Wednesday, September 17, 2003)

Professor Janis Sarra
- University of British Colombia (Thursday, September 18, 2003)

Professor Thomas Telfer
- Associate Professor of Law, University of Western Ontario (Thursday, May 29, 2003)

United Steelworkers of America
- Mr. Lawrence McBrearty, National Director (Wednesday, September 17, 2003)

Professor Roderick J. Wood
- Professor of Law, University of Alberta (Submission)

Workers' Compensation Boards
- Mr. John Solomon, Chair, Saskatchewan Workers' Compensation Board (Thursday, May 15, 2003)
- Mr. Jim Lee, Chair, P.E.I. Workers' Compensation Board (Thursday, May 15, 2003)

Workers' Compensation Boards (Cont'd)

- Mr. Douglas Mah, General Counsel, Alberta Workers' Compensation Board (Thursday, May 15, 2003)
- Mr. Maurice Cloutier, General Counsel, Quebec Commission of Occupational and Health and Safety (Thursday, May 15, 2003)

Writers' Union of Canada

- Mrs. Marian Dingman Hebb, Counsel (Thursday, May 15, 2003)
- Mrs. Deborah Windsor, Executive Director (Thursday, May 15, 2003)

Professor Jacob Ziegel

- University of Toronto (Thursday, May 29, 2003)

Professor Keith Yamauchi

- University of Calgary (Wednesday, October 1, 2003)

Ce rapport est aussi disponible en français.
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Court of Appeal File No. COA-24-CV-0468
Court File No. BK-21-02734090-0031

IN THE MATTER OF THE BANKRUPTCY AND INSOLVENCY ACT, R.S.C. 1985, c. B-3, AS AMENDED

AND IN THE MATTER OF THE NOTICES OF INTENTION TO MAKE A PROPOSAL OF YG LIMITED PARTNERSHIP AND YSL RESIDENCES INC.

COURT OF APPEAL FOR ONTARIO

PROCEEDING COMMENCED AT
TORONTO

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