CITATION: Unique Broadband Systems, Inc. v. Gerald T. McGoey, 2012 ONSC 3911
COURT FILE NO.: CV-11-9283-00CL
DATE: 2012-08-13

SUPERIOR COURT OF JUSTICE – ONTARIO

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 UNIQUE BROADBAND SYSTEMS, INC.

BEFORE: Mr. Justice H.J. Wilton-Siegel

COUNSEL: *Joseph Groia* and *Gavin Smyth*, for Jolian Investments Limited and Gerald McGoey

E. Patrick Shea and *Alexander MacFarlane*, for the Applicant, Unique Broadband Systems, Inc.

Matthew Gottlieb, for the Monitor

Peter Roy and *Alexandra Carr*, for DOL Technologies Inc. and Alex Dolgonos

Aubrey Kauffman, for Peter Minaki

S. Michael Citak, for Douglas Reeson

Michael McGraw, for Louis Mitrovich

Paul LeVay, for Malcolm Buxton-Forman

HEARD: June 13, 2012

ENDORSEMENT

[1] In these proceedings under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "CCAA"), Jolian Investments Limited ("Jolian") and Gerald McGoey ("McGoey") bring two motions: (1) seeking an order requiring that Unique Broadband Services, Inc. (the "Applicant") pay Jolian and McGoey advances in respect of their legal services pertaining to the claims determination process in the Applicant's CCAA proceedings; and (2) seeking an order or direction of this court adding certain former directors of the Applicant to the claims determination process. Similar motions were also brought by DOL Technologies Inc. ("DOL") and Alex Dolgonos ("Dolgonos") but were settled prior to the release of this Endorsement.

[2] I propose to deal with the motion for advancement first and then to deal with the motion to add the third parties.

Motion for Advancement

[3] As mentioned, Jolian and McGoey move for an order requiring the Applicant to pay advances on an interim basis pursuant to the Applicant's indemnity obligations with respect to their reasonable legal, accounting and audit expenses incurred to date since July 5, 2011, being the date of the Initial Order in these CCAA proceedings.

[4] The entitlement of the moving parties to advancement was addressed in a motion before Marrocco J. before the commencement of the CCAA proceedings. By order dated June 24, 2011, Marrocco J. ordered the Applicant to advance fees in respect of their respective legal expenses as more particularly set out therein. The present motions proceed on the basis that the order of Marrocco J. is valid.

[5] The moving parties argue that, as their claims and the Applicant's counterclaims against them are now being dealt with under the CCAA claims process, they are not obligated to seek an order lifting the stay in the Initial Order to obtain the advancement of funds to pay their legal expenses relative to these claims and counterclaims.

[6] The moving parties argue that advancement is mandatory in the present circumstances to give effect to the purpose of indemnification, as set out in *Med-Chem Health Care Ltd.* v. *Misir,* 2010 ONCA 380 (C.A.) at para. 20 and *Manitoba (Securities Commission)* v. *Crocus Investment Fund,* 2007 MBCA 36 (C.A.) at para. 50, which they say should govern notwithstanding the CCAA proceedings. They submit that the CCAA proceedings were initiated in order to avoid honoring the order of Marrocco J. They also argue that it is inequitable not to advance funds to them when the current directors are receiving an advancement of funds in respect of the claims asserted by the moving parties against them.

[7] I have sympathy for the last of these arguments. Nevertheless, I think that any claim for advancement after CCAA proceedings have been initiated constitutes a proceeding that is subject to the stay in the Initial Order. In the present case, these claims for advancement are clearly subject to the provisions of paragraph 12 of the Initial Order, as a "proceeding or enforcement process" in respect of the Marrocco J. order, and to the provisions of paragraph 13, as a "right or remedy" against the Applicant or affecting its property.

[8] Accordingly, it is necessary to consider whether the court should exercise its discretion to lift the stay and order compliance with the order of Marrocco J. The principles to be applied for such purpose are set out in the decision of Pepall J. (as she then was) in *Re Canwest Global Communications Corp.*, [2009] O.J. No. 5379 (S. Ct.) at paras. 32 and 33. As Pepall J. noted, the onus on the moving parties is a heavy one.

[9] These motions must be assessed against the current status of the Applicant. The Applicant has limited cash resources, subject to receipt of further dividends from Look Communications Inc., which are in the discretion of its board of directors, or the sale of the Applicant's investment in that company. The Applicant has no current business activities and no

income. It is subject to the CCAA proceedings because the claims of the moving parties, together with the claims of DOL and Dolgonos as of the date of the hearing of this motion, exceed the estimated value of the Applicant's assets. The claims process will determine the value of these claims and, as a corollary, the entitlement of the moving parties to indemnification, which claims will rank ahead of the claims of the shareholders.

[10] I conclude it is not appropriate to lift the stay for the following reasons.

[11] First, a significant consideration respecting the lifting of the stay from the Applicant's perspective is the effect on the assets of the Applicant and on its ability to propose a plan of reorganization based on a completed claims process. An important consideration in that regard is the need to minimize cash outlays by the Applicant in order to maximize the likelihood that it will be able to pursue the claims process through to completion.

[12] If financial hardship had been demonstrated, the court may well have had to engage in a balancing of the respective positions of the Applicant and the moving parties. However, the moving parties have not provided any financial information. Therefore, they cannot demonstrate any prejudice to them from a refusal to lift the stay. In these circumstances, the balance of convenience clearly favours the Applicant.

[13] Second, in the absence of information regarding the magnitude of the total advancement likely required in respect of the claims process and of financial information regarding the moving parties, the court is also not in a position to assess the exposure of the Applicant to the risk of non-payment if the court were to determine later that either or both of the moving parties was not entitled to indemnification.

[14] Third, while I agree that advancement would normally be ordered even in the context of a CCAA proceeding, I do not agree that advancement is mandatory in these circumstances. Notwithstanding the strong policy statements of both Canadian and American courts in favour of indemnification, I have not been provided with any case law of either jurisdiction that suggests that the policy of indemnification trumps all other considerations in a CCAA context such that advancement is absolutely required. Moreover, I do not think that is a correct proposition of law, given the additional considerations described above that come into play in a CCAA context. Each circumstance must be assessed on its own facts.

[15] Fourth, I reject the argument that, because the only activity of the Applicant is as a "litigation vehicle", the legal fees and other fees for which advancement is sought are post-filing services to the Applicant payable under the terms of the agreement between the Applicant and Jolian. The legal services are rendered to the moving parties. Insofar as they seek advancement, their entitlement remains subject to a final determination regarding their right to indemnification, failing which any monies advanced would have to be repaid. This does not reflect the characteristics of services rendered to the Applicant.

[16] Fifth, I cannot assess the merits of the moving parties' claims in the claims process, or the Applicant's claims by way of set-off. I also am not in a position to say that any actions of the Applicant, including the initiation of CCAA proceedings to avoid payment of the amounts ordered by Marrocco J., among other considerations, are such that they disentitle the Applicant from the continued benefit of the stay. This is a matter that would require a trial at a later stage in this proceeding.

[17] Based on the foregoing, the motions for advancement are denied.

Motions to Add Parties to the CCAA Proceedings

[18] Jolian and McGoey also move for an order or direction adding each of Louis Mitrovich ("Mitrovich"), Peter Minaki ("Minaki") and Douglas Reeson ("Reeson") (collectively, the "Former Directors") to the claims process in order that the claims of Jolian and McGoey against them for contribution, indemnity and misrepresentation may be determined within the CCAA claims process. A similar motion of DOL and Dolgonos to add Malcolm Buxton-Forman was adjourned.

[19] While denying any wrongdoing as alleged by the Applicant in its set-off claims in the claims process, each of the moving parties intends assert these claims against the Former Directors based on the conduct of these parties in approving the agreements and certain payments at issue in the claims process.

[20] The moving parties make three submissions. They say the Former Directors are already parties to the CCAA proceedings by virtue of their claims for indemnification in the CCAA proceedings that were filed in response to the Applicant's Counterclaim in the action commenced by Jolian and McGoey against the Applicant prior to the CCAA proceedings. They say that, without a determination of the claims against the Former Directors, the CCAA process will be lengthened considerably pending a determination of the merits of these claims outside the CCAA. Lastly, they say the Applicant has interwoven the conduct of the Former Directors into its response to the claims of Jolian and McGoey in the claims process. More generally, the moving parties argue that it will be unfair if they are forced to participate in two sets of litigation in order to determine the totality of their claims.

[21] The claims fall broadly into two categories – claims for which the Applicant seeks recovery and claims for which the Applicant asserts a right of set-off. The nature of these claimS is of some relevance to the conclusions herein.

[22] The first category comprises claims for the recovery of certain expenses for which the moving parties were reimbursed, for the recovery of certain amounts paid to their legal counsel by way of advancement of legal fees, and for damages in respect of the sale of the Canadian engineering and manufacturing business in September 2003.

[23] The damage claim has not yet been formally asserted and may never be. Accordingly, I consider it premature to address the issue of adding third parties in respect of this claim at this

time. The moving parties are at liberty to have this matter addressed by the Court if the Applicant advises that it has decided to pursue this claim on the basis of the specific claim being asserted. As the moving parties have received the monies for which recovery is sought, they can have no right to contribution in respect of any payment they may be required to make in respect of such monies.

[24] The second category of claims pertain to actions of the directors in approving the management agreement between Jolian and the Applicant and certain payments and other compensation to Jolian or McGoey. It is my understanding that the moving parties assert a claim against the Former Directors to the extent of any right of set-off found by a court to exist in favour of the Applicant in respect of such matters.

[25] Subject to the disposition of the claim regarding the sale of the manufacturing and engineering business set out above, these motions are dismissed for the following reasons.

[26] First, in the consideration of these motions, I do not accept the submission of the moving parties that the issue of joinder is governed by r. 29.01 of the *Rules of Civil Procedure*. The issue must be addressed in terms of whether joinder of the Former Directors furthers or hinders a timely and expeditious reorganization process under the CCAA pursuant to the discretion of the court under that statute.

[27] Second, the claims asserted against the Former Directors by the moving parties do not involve the Applicant directly. There is reason to doubt the authority of the court to require that disputes between creditors and third parties be determined within a claims process under a CCAA proceeding: see *Pacific Coastal Airlines Ltd.* v. *Air Canada*, [2001] B.C.J. 2580. While the present case may not fall strictly into this category of case by virtue of the contingent indemnification claims of the Former Directors, the translation of the Applicant's Counterclaim into the Claims Process would appear to render these claims moot. More generally, the court should be cautious about including third party claims, particularly where inclusion of such claims is not necessary to enable a debtor to propose a plan of reorganization. Among other considerations, such a procedure may limit or otherwise affect the rights of the third parties otherwise available under the *Rules of Civil Procedure*.

[28] Third, if it were necessary to include the claims against these parties in order to put the Applicant in a position to propose a plan of reorganization, joinder might well be necessary. However, I am satisfied that the claims against the Former Directors can proceed outside the claims process without jeopardizing the reorganization process. To the extent that such claims have not been finally resolved before consideration of a plan of reorganization, it is possible to provide for a continuation of the contingent indemnification claims of the Former Directors post-reorganization in the plan of reorganization.

[29] Fourth, joinder of the Former Directors will unnecessarily complicate the claims process, inevitably lengthening the process and making it more expensive. The result would be an

enhanced risk that the Applicant will run out of cash resources prior to completion of the claims process and submission of a plan of reorganization.

[30] Fifth, I do not think that a valid consideration is the fact that these claims arise because the Applicant has asserted that the agreement between Jolian and the Applicant, and the amounts alleged to be payable to the moving parties, are unenforceable or are invalidated because of the actions of the Former Directors. McGoey also had full knowledge of and participated in, the actions giving rise to the set-off claims. The only circumstances in which the moving parties can assert viable claims against the Former Directors would be the circumstances in which the Applicant is successful in respect of its set-off claims against the moving parties. On the other hand, to the extent the Applicant is unsuccessful in asserting these set-off claims, the moving parties will have no need to pursue the Former Directors.

[31] Sixth, the moving parties argue that the participation of the Former Directors is necessary so that they will be available as witnesses in the claims process. There are, however, other means of ensuring the presence of these parties as witnesses in these proceedings.

[32] Lastly, the issue of potentially conflicting decisions and consequential prejudice to the moving parties was raised but not fully addressed in this motion. However, I have reached the following conclusions regarding this risk that collectively indicate that the potential for prejudice is not material and should be manageable.

[33] First, in respect of the claims for the recovery of monies described above, there is no such risk as the issue will be determined by the CCAA claims process. As noted, any right of contribution will arise in favour of the Former Directors, if they satisfy any judgment in favour of the moving parties, not in favour of the moving parties. The issue of the addition of the Former Directors in respect of the damage claim has been deferred pending a further hearing if required.

[34] Second, in respect of the claims for set-off, the Applicant seeks declarations of nullity on the grounds that the agreements and other amounts alleged to be payable were not in the best interests of the Applicant or were vitiated by a conflict of interest.

[35] Given the fact that the Former Directors have knowledge of the Applicant's set-off claims in the CCAA claims process, there is a good argument that *res judicata* will operate in respect of any finding that the agreements and other amounts at issue were not in the best interests of the Applicant.

[36] The claims for nullification based on the existence of a conflict of interest fall into two categories. To the extent that a determination is made that the moving parties were themselves in a conflict of interest, I think it is probable that contribution would not be available to them in any event on the basis that they do not come before the court with clean hands.

[37] Insofar as the Former Directors, but not the moving parties, were held to have been in a conflict of interest, I acknowledge that there is a possibility of conflicting decisions to the extent

that *res judicata* does not operate. However, that risk is considerably diminished, if not excluded altogether, by the intention of Jolian and McGoey to call each of the Former Directors as witnesses. In these circumstances, the same evidentiary record should be before the court in the CCAA claims process as would be before the court in any third party proceeding brought by the moving parties for damages based on misrepresentations by the Former Directors regarding the validity of such agreements and transactions.

[38] Accordingly, the motion of Jolian and McGoey to add the Former Directors as parties in the claims process is dismissed.

Additional Issue

[39] Each of the Former Directors has also brought a motion seeking an order for advancement of their respective legal fees in the event the court were to order that they be joined as parties in the Applicant's CCAA claims process. In the circumstances, it is unnecessary to address these motions and I decline to do so.

Costs

[40] In the event the parties are unable to reach an agreement regarding the costs of these motions, they shall have thirty days to submit written cost submissions not to exceed five pages in length.

C. Wilton-Siegel J.

Wilton-Siegel J.

Date: August 13, 2012