Court File No. CV-16-11549-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF URBANCORP (WOODBINE) INC. AND URBANCORP (BRIDLEPATH) INC., THE TOWNHOUSES OF HOGG'S HOLLOW INC., KING TOWNS INC., NEWTOWNS AT KINGTOWNS INC. AND DEAJA PARTNER (BAY) INC. (COLLECTIVELY, THE "APPLICANTS")

AND IN THE MATTER OF TCC URBANCORP (BAY) LIMITED PARTNERSHIP

JOINT BOOK OF AUTHORITIES OF THE FUNCTIONARY AND TERRA FIRMA CAPITAL CORPORATION

April 20, 2018

DENTONS CANADA LLP
77 King Street West, Suite 400
Toronto, Ontario M5K 0A1
Fax: 416-863-4592

Kenneth Kraft (LSO No. 31919P)
Tel: 416-863-4374
Email: kenneth.kraft@dentons.com

Neil Rabinovitch (LSO No. 33442F)
Tel: 416-863-4656
Email: neil.rabinovitch@dentons.com

Lawyers for the Moving Party, Guy Gissin the Israeli Court-appointed functionary officer and foreign representative of Urbancorp Inc.

THORNTON GROUT FINNIGAN LLP
3200-100 Wellington Street West
TD Centre, Box 329
Toronto, ON M5K 1K7

John T. Porter (LSO No. 23844T)
Tel: (416) 304-0778
Fax: (416) 304-1313
Email: jporter@tgf.ca

Counsel for Terra Firma Capital Corporation

TO: THE SERVICE LIST

CCAA PROCEEDINGS OF URBANCORP (WOODBINE) INC., URBANCORP (BRIDLEPATH) INC. ET AL

SERVICE LIST

(UPDATED FEBRUARY 21, 2018)

TO: **DLA PIPER (CANADA) LLP**
Suite 6000, Box 367
1 First Canadian Place
Toronto, ON M5X 1E2

Edmond F.B. Lamek / Danny M. Nunes
Tel: 416.365.3444 / 416.365.3421
Email: edmond.lamek@dlapiper.com/danny.nunes@dlapiper.com

Lawyers for the Urbancorp CCAA Entities

AND TO: **KSV ADVISORY INC.**
150 King Street West, Suite 2308
Toronto, ON M5H 1J9

Bobby Kofman / Noah Goldstein / Robert Harlang
Tel: 416-932-6228 / 416-932-6027 / 416-932-6225
Email: bkofman@ksvadvisory.com / ngoldstein@ksvadvisory.com / rharlang@ksvadvisory.com

The Monitor

AND TO: **DAVIES WARD PHILLIPS & VINEBERG LLP**
155 Wellington Street West
Toronto, ON M5V 3J7

Robin B. Schwill / Jay Swartz
Tel: 416-863-5502 / 416-863-5520
Email: rschwill@dwpv.com / jswartz@dwpv.com

Lawyers for KSV Advisory Inc., in its capacity as the Monitor

AND TO: **BENNETT JONES LLP**
3400 One First Canadian Place
P.O. Box 130
Toronto, ON M5X 1A4

S. Richard Orzy / Raj S. Sahni
Tel: 416-777-5737 / 416-777-4804
Email: Orzyr@bennettjones.com / SahniR@bennettjones.com

Lawyers for Alan Saskin and Urbancorp Inc.

AND TO: **BLAKE, CASSELS & GRAYDON LLP**
199 Bay Street
Suite 4000, Commerce Court West
Toronto, ON M5L 1A9

Silvana M. D'Alimonte
Tel: 416-863-3860
Email: smda@blakes.com

Lawyers for Laurentian Bank of Canada

AND TO: **ROBINS APPLEBY LLP**
120 Adelaide Street West, Suite 2600
Toronto, ON M5H 1Tl

Leor Margulies / Dominique Michaud
Tel: 416-360-3372 / 416-360-3795
Email: lmargulies@robapp.com / dmichaud@robapp.com

THORNTON GROUT FINNIGAN LLP
Toronto-Dominion Centre
100 Wellington Street West, Suite 3200,
P.O. Box 329
Toronto, ON M5K 1K

John T. Porter
Tel: 416-304-0778
Email: jporter@tgf.ca

Co-Counsel for Terra Firma Capital Corporation

AND TO: **TEPLITSKY, COLSON LLP**
70 Bond Street, Suite 200
Toronto, ON M5B 1X3

James M. Wortzman / J. Ventrella / Catherine Allen
Tel: 416-865-5315
Email: jwortzman@teplitskycolson.com / jventrella@teplitskycolson.com / callen@teplitskycolson.com

Lawyers for Atrium Mortgage Investment Corporation

AND TO: **FOGLER, RUBINOFF LLP**
77 King Street West
TD Centre North Tower
Suite 3000, P.O. Box 95
Toronto, ON M5K I G8

Vern W. DaRe
Tel: 416-941-8842
Email: vdare@foglers.com

Lawyers for Adrian Serpa and Stefano Serpa

AND TO: **TRENT MORRIS BARRISTER**
336-20 De Boers Drive
Toronto, ON M3J OH1

Trent Morris
Tel: 647-366-6837
Email: trent@trentmorris.ca

Lawyer for six purchasers of pre-construction homes

AND TO: **TORYS LLP**
79 Wellington Street West, 30th Floor
Box 270, TD South Tower
Toronto, ON M5K 1 N2

Adam M. Slavens
Tel: 416-865-7333
Email: aslavens@torys.com

Lawyers for Tarion Warranty Corporation

AND TO: **DICKINSON WRIGHT LLP**
199 Bay Street, Suite 2200, Commerce Court
Toronto, ON M5L 1G4

Lisa Corne / David Preger
Tel: 416-646-4608 / 416-646-4606
Email: lcorne@dickinsonwright.com / dpreger@dickinsonwright.com

Lawyers for certain purchaser of pre-construction units

AND TO: **MINISTRY OF FINANCE**
77 Bay Street, 11th Floor
Toronto, ON M5G 2C8

Kevin O'Hara
Tel: 416-327-8463
Email: Kevin.Ohara@ontario.ca

AND TO: **GOLDMAN SLOAN NASH & HABER LLP**
480 University Ave Suite 1600
Toronto, Ontario M5G 1V2

Mario Forte / Robert Drake
Tel: 416-597 6477 / 416-597-5014
Email: forte@gsnh.com / drake@gsnh.com

Lawyers for Fuller Landau LLP, Proposal Trustee to Alan Saskin

AND TO: **DELZOTTO ZORZI, LLP**
4810 Dufferin Street, Suite D
Toronto, ON M3H 5S8

Robert W. Calderwood / Sabrina Adamski
Tel.: 416-665-5555
E-mail: rcalderwood@dzlaw.com / sadamski@dzlaw.com

Lawyers for Furkin Construction Inc. and GMF Consulting Inc.

AND TO: **FULLER LANDAU LLP**
151 Bloor Street West
Toronto, ON M5S 1S4

Gary Abrahamson / Adam Erlich / Ken Pearl
Tel: 416-645-6500
Email: GAbrahamson@FullerLLP.com / AErlich@FullerLLP.com / KPearl@FullerLLP.com

Proposal Trustee to Alan Saskin

AND TO: **DENTONS CANADA LLP**
400-77 King Street West, TD Centre
Toronto, ON M5K 0A1

Neil Rabinovitch / Kenneth Kraft
Tel: 416-863-4656 / 416-863-4374
Email: neil.rabinovitch@dentons.com / kenneth.kraft@dentons.com

Lawyers for Adv. Gus Gissin, in his capacity as the Court-appointed Israeli Functionary of Urbancorp Inc.

AND TO: **TORYS LLP**
79 Wellington Street West, Suite 3000
Toronto, ON M5K 1N2

Scott Bomhof
Tel: 416-865-7370
Email: sbomhof@torys.com

Lawyers for First Capital Realty Inc.

AND TO: **FARBER FINANCIAL GROUP**
150 York Street, Suite 1600
Toronto, ON M5H 3S5

Hylton Levi
Tel: 416-496-3070
Email: hlevy@farberfinancial.com

AND TO: **LAX O'SULLIVAN LISUS GOTTLIEB LLP**
Suite 2750, 145 King Street West
Toronto, ON M5H 1J8

Andrew Winton
Tel: 416.644.5342
Email: awinton@counsel-toronto.com

Lawyers for Doreen Saskin

AND TO: **CANADA REVENUE AGENCY**
c/o Department of Justice
The Exchange Tower
130 King Street West
Suite 3400, P.O. Box 36
Toronto, ON M5X 1K6

Fozia Chaudary
Tel:
Email: fozia.chaudary@justice.gc.ca

Lawyers for Canada Revenue Agency

Tor#: 3641812.3

CCAA PROCEEDINGS OF URBANCORP (WOODBINE) INC., URBANCORP (BRIDLEPATH) INC. ET AL

SERVICE LIST – email addresses
(Updated: February 21, 2018)

edmond.lamek@dlapiper.com; danny.nunes@dlapiper.com; bkofman@ksvadvisory.com; ngoldstein@ksvadvisory.com; rharlang@ksvadvisory.com; jswartz@dwpv.com; rschwill@dwpv.com; Orzyr@bennettjones.com; SahniR@bennettjones.com; smda@blakes.com; lmargulies@robapp.com; dmichaud@robapp.com; jporter@tgf.ca; jwortzman@teplitskycolson.com; jventrella@teplitskycolson.com; callen@teplitskycolson.com; vdare@foglers.com; trent@trentmorris.ca; aslavens@torys.com; lcorne@dickinsonwright.com; dpreger@dickinsonwright.com; Kevin.Ohara@ontario.ca; forte@gsnh.com; drake@gsnh.com; rcalderwood@dzlaw.com; sadamski@dzlaw.com; GAbrahamson@FullerLLP.com; AErlich@FullerLLP.com; KPearl@FullerLLP.com; neil.rabinovitch@dentons.com; kenneth.kraft@dentons.com; sbomhof@torys.com; hlevy@farberfinancial.com; awinton@counsel-toronto.com; fozia.chaudary@justice.gc.ca

Tor#: 3641812.3

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TAB 1

2010 ONSC 1708
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2010 CarswellOnt 1754, 2010 ONSC 1708, 192 A.C.W.S. (3d) 368, 63 C.B.R. (5th) 44, 81 C.C.P.B. 56

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 NORTEL NETWORKS CORPORATION, NORTEL NETWORKS LIMITED, NORTEL NETWORKS GLOBAL CORPORATION, NORTEL NETWORKS INTERNATIONAL CORPORATION AND NORTEL NETWORKS TECHNOLOGY CORPORATION (Applicants)

Morawetz J.

Heard: March 3-5, 2010
Judgment: March 26, 2010
Docket: 09-CL-7950

Counsel: Derrick Tay, Jennifer Stam, Suzanne Wood for Applicants
Lyndon Barnes, Adam Hirsh for Nortel Directors
Benjamin Zarnett, Gale Rubenstein, C. Armstrong, Melaney Wagner for Monitor, Ernst & Young Inc.
Arthur O. Jacques for Nortel Canada Current Employees
Deborah McPhail for Superintendent of Financial Services (non-PBGF)
Mark Zigler, Susan Philpott for Former and Long-Term Disability Employees
Ken Rosenberg, M. Starnino for Superintendent of Financial Services in its capacity as Administrator of the Pension Benefit Guarantee Fund
S. Richard Orzy, Richard B. Swan for Informal Nortel Noteholder Group
Alex MacFarlane, Mark Dunsmuir for Unsecured Creditors' Committee of Nortel Networks Inc.
Leanne Williams for Flextronics Inc.
Barry Wadsworth for CAW-Canada
Pamela Huff for Northern Trust Company, Canada
Joel P. Rochon, Sakie Tambakos for Opposing Former and Long-Term Disability Employees
Robin B. Schwill for Nortel Networks UK Limited (In Administration)
Sorin Gabriel Radulescu for himself
Guy Martin for himself, Marie Josee Perrault
Peter Burns for himself
Stan and Barbara Arnelien for themselves

Subject: Insolvency; Corporate and Commercial; Civil Practice and Procedure

MOTION by insolvent corporation for court approval of settlement agreement under Companies' Creditors Arrangement Act.

Morawetz J.:

Introduction

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1 On January 14, 2009, Nortel Networks Corporation ("NNC"), Nortel Networks Limited "(NNL"), Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation (collectively, the "Applicants") were granted a stay of proceedings pursuant to the *Companies' Creditors Arrangement Act* ("CCAA") and Ernst & Young Inc. was appointed as Monitor.

2 The Applicants have historically operated a number of pension, benefit and other plans (both funded and unfunded) for their employees and pensioners, including:

(i) Pension benefits through two registered pension plans, the Nortel Networks Limited Managerial and Non-Negotiated Pension Plan and the Nortel Networks Negotiated Pension Plan (the "Pension Plans"); and

(ii) Medical, dental, life insurance, long-term disability and survivor income and transition benefits paid, except for survivor termination benefits, through Nortel's Health and Welfare Trust (the "HWT").

3 Since the CCAA filing, the Applicants have continued to provide medical, dental and other benefits, through the HWT, to pensioners and employees on long-term disability ("Former and LTD Employees") and active employees ("HWT Payments") and have continued all current service contributions and special payments to the Pension Plans ("Pension Payments").

4 Pension Payments and HWT Payments made by the Applicants to the Former and LTD Employees while under CCAA protection are largely discretionary. As a result of Nortel's insolvency and the significant reduction in the size of Nortel's operations, the unfortunate reality is that, at some point, cessation of such payments is inevitable. The Applicants have attempted to address this situation by entering into a settlement agreement (the "Settlement Agreement") dated as of February 8, 2010, among the Applicants, the Monitor, the Former Employees' Representatives (on their own behalf and on behalf of the parties they represent), the LTD Representative (on her own behalf and on behalf of the parties she represents), Representative Settlement Counsel and the CAW-Canada (the "Settlement Parties").

5 The Applicants have brought this motion for approval of the Settlement Agreement. From the standpoint of the Applicants, the purpose of the Settlement Agreement is to provide for a smooth transition for the termination of Pension Payments and HWT Payments. The Applicants take the position that the Settlement Agreement represents the best efforts of the Settlement Parties to negotiate an agreement and is consistent with the spirit and purpose of the CCAA.

6 The essential terms of the Settlement Agreement are as follows:

(a) until December 31, 2010, medical, dental and life insurance benefits will be funded on a pay-as-you-go basis to the Former and LTD Employees;

(b) until December 31, 2010, LTD Employees and those entitled to receive survivor income benefits will receive income benefits on a pay-as-you-go basis;

(c) the Applicants will continue to make current service payments and special payments to the Pension Plans in the same manner as they have been doing over the course of the proceedings under the CCAA, through to March 31, 2010, in the aggregate amount of $2,216,254 per month and that thereafter and through to September 30, 2010, the Applicants shall make only current service payments to the Pension Plans, in the aggregate amount of $379,837 per month;

(d) any allowable pension claims, in these or subsequent proceedings, concerning any Nortel Worldwide Entity, including the Applicants, shall rank *pari passu* with ordinary, unsecured creditors of Nortel, and no part of any such HWT claims shall rank as a preferential or priority claim or shall be the subject of a constructive trust or trust of any nature or kind;

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(e) proofs of claim asserting priority already filed by any of the Settlement Parties, or the Superintendent on behalf of the Pension Benefits Guarantee Fund are disallowed in regard to the claim for priority;

(f) any allowable HWT claims made in these or subsequent proceedings shall rank *pari passu* with ordinary unsecured creditors of Nortel;

(g) the Settlement Agreement does not extinguish the claims of the Former and LTD Employees;

(h) Nortel and, *inter alia*, its successors, advisors, directors and officers, are released from all future claims regarding Pension Plans and the HWT, provided that nothing in the release shall release a director of the Applicants from any matter referred to in subsection 5.1(2) of the CCAA or with respect to fraud on the part of any Releasee, with respect to that Releasee only;

(i) upon the expiry of all appeals and rights of appeal in respect thereof, Representative Settlement Counsel will withdraw their application for leave to appeal the decision of the Court of Appeal, dated November 26, 2009, to the Supreme Court of Canada on a with prejudice basis; [1]

(j) a CCAA plan of arrangement in the Nortel proceedings will not be proposed or approved if that plan does not treat the Pension and HWT claimants *pari passu* to the other ordinary, unsecured creditors ("Clause H.1"); and

(k) if there is a subsequent amendment to the *Bankruptcy and Insolvency Act* ("BIA") that "changes the current, relative priorities of the claims against Nortel, no party is precluded by this Settlement Agreement from arguing the applicability" of that amendment to the claims ceded in this Agreement ("Clause H.2").

7 The Settlement Agreement does *not* relate to a distribution of the HWT as the Settlement Parties have agreed to work towards developing a Court-approved distribution of the HWT corpus in 2010.

8 The Applicants' motion is supported by the Settlement Parties and by the Board of Directors of Nortel.

9 The Official Committee of Unsecured Creditors of Nortel Networks Inc. ("UCC"), the informal Nortel Noteholder Group (the "Noteholders"), and a group of 37 LTD Employees (the "Opposing LTD Employees") oppose the Settlement Agreement.

10 The UCC and Noteholders oppose the Settlement Agreement, principally as a result of the inclusion of Clause H.2.

11 The Opposing LTD Employees oppose the Settlement Agreement, principally as a result of the inclusion of the third party releases referenced in [6h] above.

The Facts

A. Status of Nortel's Restructuring

12 Although it was originally hoped that the Applicants would be able to restructure their business, in June 2009 the decision was made to change direction and pursue sales of Nortel's various businesses.

13 In response to Nortel's change in strategic direction and the impending sales, Nortel announced on August 14, 2009 a number of organizational updates and changes including the creation of groups to support transitional services and management during the sales process.

14 Since June 2009, Nortel has closed two major sales and announced a third. As a result of those transactions, approximately 13,000 Nortel employees have been or will be transferred to purchaser companies. That includes approximately 3,500 Canadian employees.

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15 Due to the ongoing sales of Nortel's business units and the streamlining of Nortel's operations, it is expected that by the close of 2010, the Applicants' workforce will be reduced to only 475 employees. There is a need to wind-down and rationalize benefits and pension processes.

16 Given Nortel's insolvency, the significant reduction in Nortel's operations and the complexity and size of the Pension Plans, both Nortel and the Monitor believe that the continuation and funding of the Pension Plans and continued funding of medical, dental and other benefits is not a viable option.

B. The Settlement Agreement

17 On February 8, 2010 the Applicants announced that a settlement had been reached on issues related to the Pension Plans, and the HWT and certain employment related issues.

18 Recognizing the importance of providing notice to those who will be impacted by the Settlement Agreement, including the Former Employees, the LTD Employees, unionized employees, continuing employees and the provincial pension plan regulators ("Affected Parties"), Nortel brought a motion to this Court seeking the approval of an extensive notice and opposition process.

19 On February 9, 2010, this Court approved the notice program for the announcement and disclosure of the Settlement (the "Notice Order").

20 As more fully described in the Monitor's Thirty-Sixth, Thirty-Ninth and Thirty-Ninth Supplementary Reports, the Settlement Parties have taken a number of steps to notify the Affected Parties about the Settlement.

21 In addition to the Settlement Agreement, the Applicants, the Monitor and the Superintendent, in his capacity as administrator of the Pension Benefits Guarantee Fund, entered into a letter agreement on February 8, 2010, with respect to certain matters pertaining to the Pension Plans (the "Letter Agreement").

22 The Letter Agreement provides that the Superintendent will not oppose an order approving the Settlement Agreement ("Settlement Approval Order"). Additionally, the Monitor and the Applicants will take steps to complete an orderly transfer of the Pension Plans to a new administrator to be appointed by the Superintendent effective October 1, 2010. Finally, the Superintendent will not oppose any employee incentive program that the Monitor deems reasonable and necessary or the creation of a trust with respect to claims or potential claims against persons who accept directorships of a Nortel Worldwide Entity in order to facilitate the restructuring.

Positions of the Parties on the Settlement Agreement

The Applicants

23 The Applicants take the position that the Settlement is fair and reasonable and balances the interests of the parties and other affected constituencies equitably. In this regard, counsel submits that the Settlement:

(a) eliminates uncertainty about the continuation and termination of benefits to pensioners, LTD Employees and survivors, thereby reducing hardship and disruption;

(b) eliminates the risk of costly and protracted litigation regarding Pension Claims and HWT Claims, leading to reduced costs, uncertainty and potential disruption to the development of a Plan;

(c) prevents disruption in the transition of benefits for current employees;

(d) provides early payments to terminated employees in respect of their termination and severance claims where such employees would otherwise have had to wait for the completion of a claims process and distribution out of the estates;

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(e) assists with the commitment and retention of remaining employees essential to complete the Applicants' restructuring; and

(f) does not eliminate Pension Claims or HWT Claims against the Applicants, but maintains their quantum and validity as ordinary and unsecured claims.

24 Alternatively, absent the approval of the Settlement Agreement, counsel to the Applicants submits that the Applicants are not required to honour such benefits or make such payments and such benefits could cease immediately. This would cause undue hardship to beneficiaries and increased uncertainty for the Applicants and other stakeholders.

25 The Applicants state that a central objective in the Settlement Agreement is to allow the Former and LTD Employees to transition to other sources of support.

26 In the absence of the approval of the Settlement Agreement or some other agreement, a cessation of benefits will occur on March 31, 2010 which would have an immediate negative impact on Former and LTD Employees. The Applicants submit that extending payments to the end of 2010 is the best available option to allow recipients to order their affairs.

27 Counsel to the Applicants submits that the Settlement Agreement brings Nortel closer to finalizing a plan of arrangement, which is consistent with the sprit and purpose of the CCAA. The Settlement Agreement resolves uncertainties associated with the outstanding Former and LTD Employee claims. The Settlement Agreement balances certainty with clarity, removing litigation risk over priority of claims, which properly balances the interests of the parties, including both creditors and debtors.

28 Regarding the priority of claims going forward, the Applicants submit that because a deemed trust, such as the HWT, is not enforceable in bankruptcy, the Former and LTD Employees are by default *pari passu* with other unsecured creditors.

29 In response to the Noteholders' concern that bankruptcy prior to October 2010 would create pension liabilities on the estate, the Applicants committed that they would not voluntarily enter into bankruptcy proceedings prior to October 2010. Further, counsel to the Applicants submits the court determines whether a bankruptcy order should be made if involuntary proceedings are commenced.

30 Further, counsel to the Applicants submits that the court has the jurisdiction to release third parties under a Settlement Agreement where the releases (1) are connected to a resolution of the debtor's claims, (2) will benefit creditors generally and (3) are not overly broad or offensive to public policy. See *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 92 O.R. (3d) 513 (Ont. C.A.), [*Metcalfe*] at para. 71, leave to appeal refused, (S.C.C.) and *Grace Canada Inc., Re* (Ont. S.C.J. [Commercial List]) [*Grace 2008*] at para. 40.

31 The Applicants submit that a settlement of the type put forward should be approved if it is consistent with the spirit and purpose of the CCAA and is fair and reasonable in all the circumstances. Elements of fairness and reasonableness include balancing the interests of parties, including any objecting creditor or creditors, equitably (although not necessarily equally); and ensuring that the agreement is beneficial to the debtor and its stakeholders generally, as per *Air Canada, Re* (Ont. S.C.J. [Commercial List]) [*Air Canada*]. The Applicants assert that this test is met.

The Monitor

32 The Monitor supports the Settlement Agreement, submitting that it is necessary to allow the Applicants to wind down operations and to develop a plan of arrangement. The Monitor submits that the Settlement Agreement provides certainty, and does so with input from employee stakeholders. These stakeholders are represented by Employee Representatives as mandated by the court and these Employee Representatives were given the authority to approve such settlements on behalf of their constituents.

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33 The Monitor submits that Clause H.2 was bargained for, and that the employees did give up rights in order to have that clause in the Settlement Agreement; particularly, it asserts that Clause H.1 is the counterpoint to Clause H.2. In this regard, the Settlement Agreement is fair and reasonable.

34 The Monitor asserts that the court may either (1) approve the Settlement Agreement, (2) not approve the Settlement Agreement, or (3) not approve the Settlement Agreement but provide practical comments on the applicability of Clause H.2.

Former and LTD Employees

35 The Former Employees' Representatives' constituents number an estimated 19,458 people. The LTD Employees number an estimated 350 people between the LTD Employee's Representative and the CAW-Canada, less the 37 people in the Opposing LTD Employee group.

36 Representative Counsel to the Former and LTD Employees acknowledges that Nortel is insolvent, and that much uncertainty and risk comes from insolvency. They urge that the Settlement Agreement be considered within the scope of this reality. The alternative to the Settlement Agreement is costly litigation and significant uncertainty.

37 Representative Counsel submits that the Settlement Agreement is fair and reasonable for all creditors, but especially the represented employees. Counsel notes that employees under Nortel are unique creditors under these proceedings, as they are not sophisticated creditors and their personal welfare depends on receiving distributions from Nortel. The Former and LTD Employees assert that this is the best agreement they could have negotiated.

38 Representative Counsel submits that bargaining away of the right to litigate against directors and officers of the corporation, as well at the trustee of the HWT, are examples of the concessions that have been made. They also point to the giving up of the right to make priority claims upon distribution of Nortel's estate and the HWT, although the claim itself is not extinguished. In exchange, the Former and LTD Employees will receive guaranteed coverage until the end of 2010. The Former and LTD Employees submit that having money in hand today is better than uncertainty going forward, and that, on balance, this Settlement Agreement is fair and reasonable.

39 In response to allegations that third party releases unacceptably compromise employees' rights, Representative Counsel accepts that this was a concession, but submits that it was satisfactory because the claims given up are risky, costly and very uncertain. The releases do not go beyond s. 5.1(2) of the CCAA, which disallows releases relating to misrepresentations and wrongful or oppressive conduct by directors. Releases as to deemed trust claims are also very uncertain and were acceptably given up in exchange for other considerations.

40 The Former and LTD Employees submit that the inclusion of Clause H.2 was essential to their approval of the Settlement Agreement. They characterize Clause H.2 as a no prejudice clause to protect the employees by not releasing any future potential benefit. Removing Clause H.2 from the Settlement Agreement would be not the approval of an agreement, but rather the creation of an entirely new Settlement Agreement. Counsel submits that without Clause H.2, the Former and LTD Employees would not be signatories.

CAW

41 The CAW supports the Settlement Agreement. It characterizes the agreement as Nortel's recognition that it has a moral and legal obligation to its employees, whose rights are limited by the laws in this country. The Settlement Agreement temporarily alleviates the stress and uncertainty its constituents feel over the winding up of their benefits and is satisfied with this result.

42 The CAW notes that some members feel they were not properly apprised of the facts, but all available information has been disclosed, and the concessions made by the employee groups were not made lightly.

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Board of Directors

43 The Board of Directors of Nortel supports the Settlement Agreement on the basis that it is a practical resolution with compromises on both sides.

Opposing LTD Employees

44 Mr. Rochon appeared as counsel for the Opposing LTD Employees, notwithstanding that these individuals did not opt out of having Representative Counsel or were represented by the CAW. The submissions of the Opposing LTD Employees were compelling and the court extends it appreciation to Mr. Rochon and his team in co-ordinating the representatives of this group.

45 The Opposing LTD Employees put forward the position that the cessation of their benefits will lead to extreme hardship. Counsel submits that the Settlement Agreement conflicts with the spirit and purpose of the CCAA because the LTD Employees are giving up legal rights in relation to a $100 million shortfall of benefits. They urge the court to consider the unique circumstances of the LTD Employees as they are the people hardest hit by the cessation of benefits.

46 The Opposing LTD Employees assert that the HWT is a true trust, and submit that breaches of that trust create liabilities and that the claim should not be released. Specifically, they point to a $37 million shortfall in the HWT that they should be able to pursue.

47 Regarding the third party releases, the Opposing LTD Employees assert that Nortel is attempting to avoid the distraction of third party litigation, rather than look out for the best interests of the Former and LTD Employees. The Opposing LTD Employees urge the court not to release the only individuals the Former and LTD Employees can hold accountable for any breaches of trust. Counsel submits that Nortel has a common law duty to fund the HWT, which the Former and LTD Employees should be allowed to pursue.

48 Counsel asserts that allowing these releases (a) is not necessary and essential to the restructuring of the debtor, (b) does not relate to the insolvency process, (c) is not required for the success of the Settlement Agreement, (d) does not meet the requirement that each party contribute to the plan in a material way and (e) is overly broad and therefore not fair and reasonable.

49 Finally, the Opposing LTD Employees oppose the *pari passu* treatment they will be subjected to under the Settlement Agreement, as they have a true trust which should grant them priority in the distribution process. Counsel was not able to provide legal authority for such a submission.

50 A number of Opposing LTD Employees made in person submissions. They do not share the view that Nortel will act in their best interests, nor do they feel that the Employee Representatives or Representative Counsel have acted in their best interests. They shared feelings of uncertainty, helplessness and despair. There is affidavit evidence that certain individuals will be unable to support themselves once their benefits run out, and they will not have time to order their affairs. They expressed frustration and disappointment in the CCAA process.

UCC

51 The UCC was appointed as the representative for creditors in the U.S. Chapter 11 proceedings. It represents creditors who have significant claims against the Applicants. The UCC opposes the motion, based on the inclusion of Clause H.2, but otherwise the UCC supports the Settlement Agreement.

52 Clause H.2, the UCC submits, removes the essential element of finality that a settlement agreement is supposed to include. The UCC characterizes Clause H.2 as a take back provision; if activated, the Former and LTD Employees have compromised nothing, to the detriment of other unsecured creditors. A reservation of rights removes the finality of the Settlement Agreement.

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53 The UCC claims it, not Nortel, bears the risk of Clause H.2. As the largest unsecured creditor, counsel submits that a future change to the BIA could subsume the UCC's claim to the Former and LTD Employees and the UCC could end up with nothing at all, depending on Nortel's asset sales.

Noteholders

54 The Noteholders are significant creditors of the Applicants. The Noteholders oppose the settlement because of Clause H.2, for substantially the same reasons as the UCC.

55 Counsel to the Noteholders submits that the inclusion of H.2 is prejudicial to the non-employee unsecured creditors, including the Noteholders. Counsel submits that the effect of the Settlement Agreement is to elevate the Former and LTD Employees, providing them a payout of $57 million over nine months while everyone else continues to wait, and preserves their rights in the event the laws are amended in future. Counsel to the Noteholders submits that the Noteholders forego millions of dollars while remaining exposed to future claims.

56 The Noteholders assert that a proper settlement agreement must have two elements: a real compromise, and resolution of the matters in contention. In this case, counsel submits that there is no resolution because there is no finality in that Clause H.2 creates ambiguity about the future. The very object of a Settlement Agreement, assert the Noteholders, is to avoid litigation by withdrawing claims, which this agreement does not do.

Superintendent

57 The Superintendent does not oppose the relief sought, but this position is based on the form of the Settlement Agreement that is before the Court.

Northern Trust

58 Northern Trust, the trustee of the pension plans and HWT, takes no position on the Settlement Agreement as it takes instructions from Nortel. Northern Trust indicates that an oversight left its name off the third party release and asks for an amendment to include it as a party released by the Settlement Agreement.

Law and Analysis

A. Representation and Notice Were Proper

59 It is well settled that the Former Employees' Representatives and the LTD Representative (collectively, the "Settlement Employee Representatives") and Representative Counsel have the authority to represent the Former Employees and the LTD Beneficiaries for purposes of entering into the Settlement Agreement on their behalf: *see Grace 2008*, *supra* at para 32.

60 The court appointed the Settlement Employee Representatives and the Representative Settlement Counsel. These appointment orders have not been varied or appealed. Unionized employees continue to be represented by the CAW. The Orders appointing the Settlement Employee Representatives expressly gave them authority to represent their constituencies "for the purpose of settling or compromising claims" in these Proceedings. Former Employees and LTD Employees were given the right to opt out of their representation by Representative Settlement Counsel. After provision of notice, only one former employee and one active employee exercised the opt-out right.

B. Effect of the Settlement Approval Order

61 In addition to the binding effect of the Settlement Agreement, many additional parties will be bound and affected by the Settlement Approval Order. Counsel to the Applicants submits that the binding nature of the Settlement Approval

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Order on all affected parties is a crucial element to the Settlement itself. In order to ensure all Affected Parties had notice, the Applicants obtained court approval of their proposed notice program.

62 Even absent such extensive noticing, virtually all employees of the Applicants are represented in these proceedings. In addition to the representative authority of the Settlement Employee Representatives and Representative Counsel as noted above, Orders were made authorizing a Nortel Canada Continuing Employees' Representative and Nortel Canada Continuing Employees' Representative Counsel to represent the interests of continuing employees on this motion.

63 I previously indicated that "the overriding objective of appointing representative counsel for employees is to ensure that the employees have representation in the CCAA process": *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) at para 16. I am satisfied that this objective has been achieved.

64 The Record establishes that the Monitor has undertaken a comprehensive notice process which has included such notice to not only the Former Employees, the LTD Employees, the unionized employees and the continuing employees but also the provincial pension regulators and has given the opportunity for any affected person to file Notices of Appearance and appear before this court on this motion.

65 I am satisfied that the notice process was properly implemented by the Monitor.

66 I am satisfied that Representative Counsel has represented their constituents' interests in accordance with their mandate, specifically, in connection with the negotiation of the Settlement Agreement and the draft Settlement Approval Order and appearance on this Motion. There have been intense discussions, correspondence and negotiations among Representative Counsel, the Monitor, the Applicants, the Superintendent, counsel to the Board of the Applicants, the Noteholder Group and the Committee with a view to developing a comprehensive settlement. NCCE's Representative Counsel have been apprised of the settlement discussions and served with notice of this Motion. Representatives have held Webinar sessions and published press releases to inform their constituents about the Settlement Agreement and this Motion.

C. Jurisdiction to Approve the Settlement Agreement

67 The CCAA is a flexible statute that is skeletal in nature. It has been described as a "sketch, an outline, a supporting framework for the resolution of corporate insolvencies in the public interest". *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) at paras. 28-29, citing *Metcalfe*, *supra*, at paras. 44 and 61.

68 Three sources for the court's authority to approve pre-plan agreements have been recognized:

(a) the power of the court to impose terms and conditions on the granting of a stay under s. 11(4) of the CCAA;

(b) the power of the court to make an order "on such terms as it may impose" pursuant to s. 11(4) of the CCAA; and

(c) the inherent jurisdiction of the court to "fill in the gaps" of the CCAA in order to give effect to its objects: see *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) at para. 30, citing *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (Ont. Gen. Div. [Commercial List]) [*Canadian Red Cross*] at para. 43; *Metcalfe*, *supra* at para. 44.

69 In *Stelco Inc., Re* (2005), 78 O.R. (3d) 254 (Ont. C.A.), the Ontario Court of Appeal considered the court's jurisdiction under the CCAA to approve agreements, determining at para. 14 that it is not limited to preserving the *status quo*. Further, agreements made prior to the finalization of a plan or compromise are valid orders for the court to approve: *Grace 2008*, *supra* at para. 34.

70 In these proceedings, this court has confirmed its jurisdiction to approve major transactions, including settlement agreements, during the stay period defined in the Initial Order and prior to the proposal of any plan of compromise or

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arrangement: see, for example, *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]); *Nortel Networks Corp., Re* (Ont. S.C.J. [Commercial List]) and *Nortel Networks Corp., Re*, 2010 ONSC 1096 (Ont. S.C.J. [Commercial List]).

71 I am satisfied that this court has jurisdiction to approve transactions, including settlements, in the course of overseeing proceedings during a CCAA stay period and prior to any plan of arrangement being proposed to creditors: see *Calpine Canada Energy Ltd., Re* (Alta. C.A. [In Chambers]) [*Calpine*] at para. 23, affirming (Alta. Q.B.); *Canadian Red Cross, supra*; *Air Canada, supra*; *Grace 2008, supra*, and *Grace Canada Inc., Re* (Ont. S.C.J. [Commercial List]) [*Grace 2010*], leave to appeal to the C.A. refused February 19, 2010; *Nortel Networks Corp., Re*, 2010 ONSC 1096 (Ont. S.C.J. [Commercial List]).

D. Should the Settlement Agreement Be Approved?

72 Having been satisfied that this court has the jurisdiction to approve the Settlement Agreement, I must consider whether the Settlement Agreement *should* be approved.

73 A Settlement Agreement can be approved if it is consistent with the spirit and purpose of the CCAA and is fair and reasonable in all circumstances. What makes a settlement agreement fair and reasonable is its balancing of the interests of all parties; its equitable treatment of the parries, including creditors who are not signatories to a settlement agreement; and its benefit to the Applicant and its stakeholders generally.

i) Sprit and Purpose

74 The CCAA is a flexible instrument; part of its purpose is to allow debtors to balance the conflicting interests of stakeholders. The Former and LTD Employees are significant creditors and have a unique interest in the settlement of their claims. This Settlement Agreement brings these creditors closer to ultimate settlement while accommodating their special circumstances. It is consistent with the spirit and purpose of the CCAA.

ii) Balancing of Parties' Interests

75 There is no doubt that the Settlement Agreement is comprehensive and that it has support from a number of constituents when considered in its totality.

76 There is, however, opposition from certain constituents on two aspects of the proposed Settlement Agreement: (1) the Opposing LTD Employees take exception to the inclusion of the third party releases; (2) the UCC and Noteholder Groups take exception to the inclusion of Clause H.2.

Third Party Releases

77 Representative Counsel, after examining documentation pertaining to the Pension Plans and HWT, advised the Former Employees' Representatives and Disabled Employees' Representative that claims against directors of Nortel for failing to properly fund the Pension Plans were unlikely to succeed. Further, Representative Counsel advised that claims against directors or others named in the Third Party Releases to fund the Pension Plans were risky and could take years to resolve, perhaps unsuccessfully. This assisted the Former Employees' Representatives and the Disabled Employees' Representative in agreeing to the Third Party Releases.

78 The conclusions reached and the recommendations made by both the Monitor and Representative Counsel are consistent. They have been arrived at after considerable study of the issues and, in my view, it is appropriate to give significant weight to their positions.

79 In *Grace 2008, supra*, and *Grace 2010, supra*, I indicated that a Settlement Agreement entered into with Representative Counsel that contains third party releases is fair and reasonable where the releases are necessary and connected to a resolution of claims against the debtor, will benefit creditors generally and are not overly broad or offensive to public policy.

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80 In this particular case, I am satisfied that the releases are necessary and connected to a resolution of claims against the Applicants.

81 The releases benefit creditors generally as they reduces the risk of litigation against the Applicants and their directors, protect the Applicants against potential contribution claims and indemnity claims by certain parties, including directors, officers and the HWT Trustee; and reduce the risk of delay caused by potentially complex litigation and associated depletion of assets to fund potentially significant litigation costs.

82 Further, in my view, the releases are not overly broad or offensive to public policy. The claims being released specifically relate to the subject matter of the Settlement Agreement. The parties granting the release receive consideration in the form of both immediate compensation and the maintenance of their rights in respect to the distribution of claims.

Clause H.2

83 The second aspect of the Settlement Agreement that is opposed is the provision known as Clause H.2. Clause H.2 provides that, in the event of a bankruptcy of the Applicants, and notwithstanding any provision of the Settlement Agreement, if there are any amendments to the BIA that change the current, relative priorities of the claims against the Applicants, no party is precluded from arguing the applicability or non-applicability of any such amendment in relation to any such claim.

84 The Noteholders and UCC assert that Clause H.2 causes the Settlement Agreement to not be a "settlement" in the true and proper sense of that term due to a lack of certainty and finality. They emphasize that Clause H.2 has the effect of undercutting the essential compromises of the Settlement Agreement in imposing an unfair risk on the non-employee creditors of NNL, including NNI, after substantial consideration has been paid to the employees.

85 This position is, in my view, well founded. The inclusion of the Clause H.2 creates, rather than eliminates, uncertainty. It creates the potential for a fundamental alteration of the Settlement Agreement.

86 The effect of the Settlement Agreement is to give the Former and LTD Employees preferred treatment for certain claims, notwithstanding that priority is not provided for in the statute nor has it been recognized in case law. In exchange for this enhanced treatment, the Former Employees and LTD Beneficiaries have made certain concessions.

87 The Former and LTD Employees recognize that substantially all of these concessions could be clawed back through Clause H.2. Specifically, they acknowledge that future Pension and HWT Claims will rank *pari passu* with the claims of other ordinary unsecured creditors, but then go on to say that should the BIA be amended, they may assert once again a priority claim.

88 Clause H.2 results in an agreement that does not provide certainty and does not provide finality of a fundamental priority issue.

89 The Settlement Parties, as well as the Noteholders and the UCC, recognize that there are benefits associated with resolving a number of employee-related issues, but the practical effect of Clause H.2 is that the issue is not fully resolved. In my view, Clause H.2 is somewhat inequitable from the standpoint of the other unsecured creditors of the Applicants. If the creditors are to be bound by the Settlement Agreement, they are entitled to know, with certainty and finality, the effect of the Settlement Agreement.

90 It is not, in my view, reasonable to require creditors to, in effect, make concessions in favour of the Former and LTD Employees today, and be subject to the uncertainty of unknown legislation in the future.

91 One of the fundamental purposes of the CCAA is to facilitate a process for a compromise of debt. A compromise needs certainty and finality. Clause H.2 does not accomplish this objective. The inclusion of Clause H.2 does not recognize that at some point settlement negotiations cease and parties bound by the settlement have to accept the

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outcome. A comprehensive settlement of claims in the magnitude and complexity contemplated by the Settlement Agreement should not provide an opportunity to re-trade the deal after the fact.

92 The Settlement Agreement should be fair and reasonable in all the circumstances. It should balance the interests of the Settlement Parties and other affected constituencies equitably and should be beneficial to the Applicants and their stakeholders generally.

93 It seems to me that Clause H.2 fails to recognize the interests of the other creditors of the Applicants. These creditors have claims that rank equally with the claims of the Former Employees and LTD Employees. Each have unsecured claims against the Applicants. The Settlement Agreement provides for a transfer of funds to the benefit of the Former Employees and LTD Employees at the expense of the remaining creditors. The establishment of the Payments Charge crystallized this agreed upon preference, but Clause H.2 has the effect of not providing any certainty of outcome to the remaining creditors.

94 I do not consider Clause H.2 to be fair and reasonable in the circumstances.

95 In light of this conclusion, the Settlement Agreement cannot be approved in its current form.

96 Counsel to the Noteholder Group also made submissions that three other provisions of the Settlement Agreement were unreasonable and unfair, namely:

(i) ongoing exposure to potential liability for pension claims if a bankruptcy order is made before October 1, 2010;

(ii) provisions allowing payments made to employees to be credited against employees' claims made, rather than from future distributions or not to be credited at all; and

(iii) lack of clarity as to whether the proposed order is binding on the Superintendent in all of his capacities under the *Pension Benefits Act* and other applicable law, and not merely in his capacity as Administrator on behalf of the Pension Benefits Guarantee Fund.

97 The third concern was resolved at the hearing with the acknowledgement by counsel to the Superintendent that the proposed order would be binding on the Superintendent in all of his capacities.

98 With respect to the concern regarding the potential liability for pension claims if a bankruptcy order is made prior to October 1, 2010, counsel for the Applicants undertook that the Applicants would not take any steps to file a voluntary assignment into bankruptcy prior to October 1, 2010. Although such acknowledgment does not bind creditors from commencing involuntary bankruptcy proceedings during this time period, the granting of any bankruptcy order is preceded by a court hearing. The Noteholders would be in a position to make submissions on this point, if so advised. This concern of the Noteholders is not one that would cause me to conclude that the Settlement Agreement was unreasonable and unfair.

99 Finally, the Noteholder Group raised concerns with respect to the provision which would allow payments made to employees to be credited against employees' claims made, rather than from future distributions, or not to be credited at all. I do not view this provision as being unreasonable and unfair. Rather, it is a term of the Settlement Agreement that has been negotiated by the Settlement Parties. I do note that the proposed treatment with respect to any payments does provide certainty and finality and, in my view, represents a reasonable compromise in the circumstances.

Disposition

100 I recognize that the proposed Settlement Agreement was arrived at after hard-fought and lengthy negotiations. There are many positive aspects of the Settlement Agreement. I have no doubt that the parties to the Settlement Agreement consider that it represents the best agreement achievable under the circumstances. However, it is my conclusion that the inclusion of Clause H.2 results in a flawed agreement that cannot be approved.

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101 I am mindful of the submission of counsel to the Former and LTD Employees that if the Settlement Agreement were approved, with Clause H.2 excluded, this would substantively alter the Settlement Agreement and would, in effect, be a creation of a settlement and not the approval of one.

102 In addition, counsel to the Superintendent indicated that the approval of the Superintendent was limited to the proposed Settlement Agreement and would not constitute approval of any altered agreement.

103 In *Grace 2008, supra*, I commented that a line-by-line analysis was inappropriate and that approval of a settlement agreement was to be undertaken in its entirety or not at all, at para. 74. A similar position was taken by the New Brunswick Court of Queen's Bench in *Wandlyn Inns Limited (Re)* (1992), 15 C.B.R. (3d) 316 (N.B. Q.B.). I see no reason or basis to deviate from this position.

104 Accordingly, the motion is dismissed.

105 In view of the timing of the timing of the release of this decision and the functional funding deadline of March 31, 2010, the court will make every effort to accommodate the parties if further directions are required.

106 Finally, I would like to express my appreciation to all counsel and in person parties for the quality of written and oral submissions.

Motion dismissed.

Footnotes

1 On March 25, 2010, the Supreme Court of Canada released the following: *Donald Sproule et al. v. Nortel Networks Corporation et al.* (Ont.) (Civil) (By Leave) (33491) (The motions for directions and to expedite the application for leave to appeal are dismissed. The application for leave to appeal is dismissed with no order as to costs./La requête en vue d'obtenir des directives et la requête visant à accélérer la procédure de demande d'autorisation d'appel sont rejetées. La demande d'autorisation d'appel est rejetée; aucune ordonnance n'est rendue concernant les dépens.): <http://scc.lexum.umontreal.ca/en/news_release/2010/10-03-25.3a/10-03-25.3a.html>

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TAB 2

2007 ABCA 266
Alberta Court of Appeal (In Chambers)

Calpine Canada Energy Ltd., Re

2007 CarswellAlta 1097, 2007 ABCA 266, [2007] A.W.L.D. 3481, [2007] A.J. No. 917, 161 A.C.W.S. (3d) 370, 33 B.L.R. (4th) 94, 35 C.B.R. (5th) 27, 410 W.A.C. 25, 417 A.R. 25, 80 Alta. L.R. (4th) 60

In the Matter of the Companies Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

And In the Matter of Calpine Canada Energy Limited, Calpine Canada Power Ltd., Calpine Canada Energy Finance ULC, Calpine Energy Services Canada Ltd., Calpine Canada Resources Company, Calpine Canada Power Services Ltd., Calpine Canada Energy Finance II ULC, Calpine Natural Gas Services Limited and 3094479 Nova Scotia Company (the "CCAA Applicants")

Calpine Power L.P. (Appellant / Applicant (Creditor)) and The CCAA Applicants and Calpine Energy Services Canada Partnership, Calpine Canada Natural Gas Partnership and Calpine Canadian Saltend Limited Partnership (Respondents / Applicants)

Calpine Canada Natural Gas Partnership (Respondent / Applicant / CCAA Party) and Calpine Energy Services Canada Partnership and Lisa Winslow, Trustee of Calpine Greenfield Commercial Trust (Respondents / (CCAA Applicant and Interested Parties)) and Calpine Power L.P. (Appellant / Applicant / (Creditor in CCAA Proceedings))

C. O'Brien J.A.

Heard: August 15, 2007
Judgment: August 17, 2007
Docket: Calgary Appeal 0701-0222-AC, 0701-0223-AC

Proceedings: refusing leave to appeal *Calpine Canada Energy Ltd., Re* (2007), 2007 CarswellAlta 1050, 2007 ABQB 504 (Alta. Q.B.)

Counsel: P.T. Linder, Q.C., R. Van Dorp for Applicant, CPL
L.B. Robinson, Q.C., S.F. Collins, J.A. Carfagnini for CCAA Applicants and the CCAA Parties (Respondents)
H.A. Gorman for Ad Hoc ULCI Noteholders Committee
P.H. Griffin, U. Sheikh for Calpine Corporation and other US Debtors
F.R. Dearlove for HSBC
P. McCarthy, Q.C., J. Kruger for Ernst & Young Inc., the Monitor
N.S. Rabinovitch for Lien Debtholders
R. De Waal for Unsecured Creditors Committee

Subject: Insolvency

APPLICATION by creditor for stay pending appeal and leave to appeal from judgment reported at *Calpine Canada Energy Ltd., Re* (2007), 2007 CarswellAlta 1050, 2007 ABQB 504, 35 C.B.R. (5th) 1, 33 B.L.R. (4th) 68 (Alta. Q.B.), granting application for approval of settlement.

C. O'Brien J.A.:

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Introduction

1 Calpine Power L.P. (CLP) applies for a stay pending appeal and leave to appeal three orders granted on July 24, 2007 in a proceeding under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36, as amended (CCAA). At the request of counsel, the applications have been dealt with on an expedited basis. Oral submissions were heard on August 15, at the close of which I undertook to deliver judgment by the end of the week. I do so now.

Background facts

2 In December 2005, Calpine Canada Energy Limited, Calpine Canada Power Ltd., Calpine Canada Energy Finance ULC, Calpine Energy Services Canada Ltd., Calpine Canada Resources Company, Calpine Canada Power Services Ltd., Calpine Canada Energy Finance II ULC, Calpine Natural Gas Services Limited, and 3094479 Nova Scotia Company (CCAA Applicants) sought and obtain protection under the CCAA. At the same time, the parties referred to as the US Debtors sought and obtained similar protection under Chapter 11 of the U. S. Bankruptcy Code.

3 A monitor, Ernst & Young Inc., was appointed under the CCAA proceedings and a stay of proceedings was ordered against the CCAA Applicants and against Calpine Energy Services Canada Partnership, Calpine Canada Natural Gas Partnership and Calpine Canadian Saltend Limited Partnership. The latter three parties collectively are referred to as the CCAA Parties and those parties together with the CCAA Applicants as the CCAA Debtors.

4 This insolvency is extremely complex, involving many related corporations and partnerships, and highly intertwined legal and financial obligations. The goal of restructuring and realizing maximum value for assets has been made more difficult by a number of cross-border issues.

5 As described in the Monitor's 23rd Report, dated June 28, 2007, the CCAA Debtors and the US Debtors concluded that the most appropriate way to resolve the issues between them was to concentrate on reaching a consensual global agreement that resolved virtually all the material cross-border issues between them. The parties negotiated a global settlement agreement (GSA) subject to the approval of both Canadian and U. S. courts, execution of the GSA and the sale by Calpine Canada Resources Company of its holdings of Calpine Canada Energy Finance ULC (ULC1) Notes in the face amount of US$359,770,000 (the CCRC ULC1 Notes). Counsel at the oral hearing informed me that the Notes were sold on August 14, 2007, yielding a net amount of approximately US $403 million, an amount exceeding the face amount.

6 On July 24, 2007, the CCAA Applicants sought and obtained three orders. First, an order approving the terms of the GSA and directing the various parties to execute such documents and implement the transactions necessary to give effect to the GSA. Second, an order permitting CCRC and ULC1 to take the necessary steps to sell the CCRC ULC1 Notes. Third, an extension of the stay contemplated by the initial CCAA order to December 20, 2007. No objection was taken to the latter two orders and both were granted. The supervising judge also, in brief oral reasons, approved the GSA with written reasons to follow. Written Reasons for Judgment were subsequently filed on July 31, 2007: *Calpine Canada Energy Ltd., Re*, 2007 ABQB 504 (Alta. Q.B.). The reasons are careful and detailed. They fully set out the relevant facts and canvas the applicable law and as I see no need to repeat the facts and authorities, the reasons should be read in conjunction with these relatively short reasons dealing with the applications arising therefrom.

7 The applications to the supervising judge were made concurrently with applications by the US Debtors to the US Bankruptcy Court in New York state, the applications proceeding simultaneously by video conference. The applications to the US Court, including an application for approval of the GSA, were also granted.

8 The applicant, CLP, the Calpine Canada Energy Finance II ULC (ULC2) Indenture Trustee and a group referring to itself as the "Ad Hoc Committee of Creditors of Calpine Canada Resources Company" opposed the approval of the GSA. CPL is the only party seeking leave to appeal.

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9 CLP submits that the supervising judge erred in concluding that the GSA was not a compromise or plan of arrangement and therefore, sections 4 and 5 of the CCAA did not apply and no vote by creditors was necessary.

10 Sections 4 and 5 of the CCAA provide:

> 4. Where a compromise or an arrangement is proposed between a debtor company and its unsecured creditors or any class of them, the court may, on the application in a summary way of the company, of any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors, and, if the court so determines, of the shareholders of the company, to be summoned in such manner as the court directs.
>
> 5. Where a compromise or an arrangement is proposed between a debtor company and its secured creditors or any class of them, the court may, on the application in a summary way of the company or of any such creditor or of the trustee in bankruptcy or liquidator of the company, order a meeting of the creditors or class of creditors, and, if the court so determines, of the shareholders of the company, to be summoned in such manner as the court directs.

11 CLP further submits that the jurisdiction of the supervising judge to approve the GSA is governed by section 6 of the CCAA. Section 6 provides:

> Where a majority in number representing two-thirds in value of the creditors, or class of creditors, as the case may be, present and voting either in person or by proxy at the meeting or meetings thereof respectively held pursuant to sections 4 and 5, or either of those sections, agree to any compromise or arrangement either as proposed or as altered or modified at the meeting or meetings, the compromise or arrangement may be sanctioned by the court, and if so sanctioned is binding
>
> > (a) on all the creditors or the class of creditors, as the case may be, and on any trustee for any such class of creditors, whether secured or unsecured, as the case may be, and on the company; and
> >
> > (b) in the case of a company that has made an authorized assignment or against which a bankruptcy order has been made under the Bankruptcy and Insolvency Act or is in the course of being wound up under the Winding-up and Restructuring Act, on the trustee in bankruptcy or liquidator and contributories of the company.

12 The supervising judge found that the GSA is not linked to or subject to a plan of arrangement and does not compromise the rights of creditors that are not parties to it or have not consented to it, and it does not have the effect of unilaterally depriving creditors of contractual rights without their participation in the GSA. She concluded that the GSA was not a compromise or arrangement for the purposes of section 4 of the CCAA. In the course of her reasons she cites a number of cases for support that the court has jurisdiction to review and approve transactions and settlement agreements during the stay period of a CCAA proceedings if an agreement is fair and reasonable and will be beneficial to the debtor and its stakeholders generally.

Test for leave to appeal

13 This Court has repeatedly stated, for example in *Liberty Oil & Gas Ltd., Re*, 2003 ABCA 158, 44 C.B.R. (4th) 96 (Alta. C.A.), at paras. 15-16, that the test for leave under the CCAA involves a single criterion that there must be serious and arguable grounds that are of real and significant interest to the parties. The four factors used to assess whether this criterion is present are:

> (1) Whether the point on appeal is of significance to the practice;
>
> (2) Whether the point raised is of significance to the action itself;
>
> (3) Whether the appeal is *prima facie* meritorious or, on the other hand, whether it is frivolous; and

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(4) Whether the appeal will unduly hinder the progress of the action.

14 In assessing these factors, consideration should also be given to the applicable standard of review: *Canadian Airlines Corp., Re*, 2000 ABCA 149, 261 A.R. 120 (Alta. C.A. [In Chambers]). Having regard to the commercial nature of the proceedings which often require quick decisions, and to the intimate knowledge acquired by a supervising judge in overseeing a CCAA proceedings, appellate courts have expressed a reluctance to interfere, except in clear cases: *Smoky River Coal Ltd., Re*, 1999 ABCA 179, 237 A.R. 326 (Alta. C.A.) at para. 61.

Analysis

15 The standard of review plays a significant, if not decisive, role in the outcome of this application for leave to appeal. The supervising judge, on the record of evidence before her, found that the GSA was "not a plan of compromise or arrangement with creditors" (Reasons, para. 51). This was a finding of fact, or at most, a finding of mixed law and fact. The applicant has identified no extricable error of law so the applicable standard is palpable or overriding error.

16 The statute itself contains no definition of a compromise or arrangement. Moreover, it does not appear that a compromise or an arrangement has been *proposed* between a debtor company and either its unsecured or secured creditors, or any class of them within the scope of sections 4 or 5 of the CCAA. Neither the company, a creditor, nor anyone made application to convene a meeting under those sections.

17 Rather, the GSA settles certain intercorporate claims between certain Canadian Calpine entities and certain US Calpine entities subject to certain conditions, including the approvals both of the Court of Queen's Bench of Alberta and of the US Bankruptcy Court.

18 This is not to minimize the magnitude, significance and complexity of the issues dealt with in the intercorporate settlement which, by definition, was not between arm's length companies. The material cross-border issues are identified in the 23rd Report of the monitor and listed by the supervising judge (Reasons, para. 5).

19 It is implicit in her reasons, if not express, that the supervising judge accepted the analysis of the monitor, and found that the GSA would likely ultimately result in payment in full of all Canadian creditors, including CLP. CLP does not challenge this finding, but points out that payment is not assured, and rightly relies upon its status as a creditor to challenge the approval in the meantime until such time as it has been paid.

20 The supervising judge further found that the GSA "does not compromise the rights of creditors that are not parties to it or have not consented to it, and it certainly does not have the effect of unilaterally depriving creditors of contractual rights without their participation in the GSA" (Reasons, para. 51). CPL challenges this finding. In order to succeed in its proposed appeal, CPL must also demonstrate palpable and overriding error in these further findings of the supervising judge which once again, involve findings of fact or of mixed law and fact.

Application in this case

21 CPL submits that the "fundamental problem" with the approval granted by the supervising judge is that the GSA is in reality a plan of arrangement because it settles virtually all matters in dispute in the Canadian CCAA estate and therefore, entitles the applicant to a vote. CPL argues that the GSA must be an arrangement or compromise within the meaning of sections 4, 5 and 6 of the CCAA because, in its view, the GSA requires non party creditors to make concessions, re-orders the priorities of creditors and distributes assets of the estate.

22 The supervising judge acknowledged at the outset of her analysis that if the GSA were a plan of arrangement or compromise, a vote by creditors would be necessary (Reasons, para. 41). However, she was satisfied that the GSA did not constitute a plan of arrangement with creditors.

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23 The applicant conceded that a CCAA supervising judge has jurisdiction to approve transactions, including settlements in the course of overseeing proceedings during a stay period and prior to any plan of arrangement being proposed to creditors. This concession was proper having regard to case authority recognizing such jurisdiction and cited in the reasons of the supervising judge, including *Air Canada, Re* (2004), 47 C.B.R. (4th) 169 (Ont. S.C.J. [Commercial List]), *Playdium Entertainment Corp., Re* (2001), 31 C.B.R. (4th) 302 (Ont. S.C.J. [Commercial List]), *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]), *T. Eaton Co., Re* (1999), 14 C.B.R. (4th) 288 (Ont. S.C.J. [Commercial List]) and *Stelco Inc., Re* (2005), 78 O.R. (3d) 254 (Ont. C.A.).

24 The power to approve such transactions during the stay is not spelled out in the CCAA. As has often been observed, the statute is skeletal. The approval power in such instances is usually said to be found either in the broad powers under section 11(4) to make orders other than on an initial application to effectuate the stay, or in the court's inherent jurisdiction to fill in gaps in legislation so as to give effect to the objects of the CCAA, including the survival program of the debtor until it can present a plan: *Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Gen. Div. [Commercial List]) at para. 8.

25 Hunt, J.A. in delivering the judgment of this Court in *Smoky River Coal*considered the history of the legislation and its objectives in allowing the company to take steps to promote a successful eventual arrangement. She concluded at para. 53:

> These statements about the goals and operation of the CCAA support the view that the discretion under s. 11(4) should be interpreted widely.

and further at para. 60:

> To summarize, the language of s. 11(4) is very broad. The CCAA must be interpreted in a remedial fashion.

26 In my view, there is no serious issue as to the jurisdiction of a supervising judge to approve a settlement agreement between consenting parties prior to consideration of a plan of arrangement pursuant to section 6 of the CCAA. The fact that the GSA is not a simple agreement between two parties, but rather resolves a number of complex issues between a number of parties, does not affect the jurisdiction of the court to approve the agreement if it is for the general benefit of all parties and otherwise meets the tests identified in the reasons of the supervising judge.

27 CPL urges that the legal issue for determination by this Court is where the line is to be drawn to say when a settlement becomes a compromise or arrangement, thus requiring a vote under section 6 before the court can grant approval. It suggests that it would be useful to this practice area for the court to set out the criteria to be considered in this regard.

28 An element of compromise is inherent in a settlement as there is invariably some give and take by the parties in reaching their agreement. The parties to the GSA made concessions for the purpose of gaining benefits. It is obvious that something more than compromise between consenting parties within a settlement agreement is required to constitute an arrangement or compromise for purposes of the CCAA as if that were not so, no settlement agreement could be approved without a vote of the creditors. As noted, that is contrary to case authority accepted by all parties to these applications.

29 The CCAA deals with compromises or arrangements sought to be imposed upon creditors generally, or classes of creditors, and a vote is a necessary mechanism to determine whether the appropriate majority of the creditors proposed to be affected support the proposed compromise or arrangement.

30 As pointed out by the supervising judge, a settlement will almost always have an impact on the financial circumstances of a debtor. A settlement will invariably have an effect on the size of the estate available for other claimants (Reasons, para. 62).

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31 Whether or not a settlement constitutes a plan of arrangement requiring a vote will be dependent upon the factual circumstances of each case. Here, the supervising judge carefully reviewed the circumstances and concluded, on the basis of a number of the fact findings, that there was no plan of arrangement within the meaning of the CCAA, and that the settlement merited approval. She recognized the peculiar circumstances which distinguishes this case, and observed at para. 76 of her Reasons:

> The precedential implications of this approval must be viewed in the context of the unique circumstances that have presented a situation in which all valid claims of Canadian creditors likely will be paid in full. This outcome, particularly with respect to a cross-border insolvency of exceptional complexity, is unlikely to be matched in other insolvencies, and therefore, a decision to approve this settlement agreement will not open any floodgates.

32 At the time of granting her approval, the supervising judge had been overseeing the conduct of these CCAA proceedings since their inception — some 18 months earlier. She had the benefit of the many reports of the monitor and was familiar with the record of the proceedings. Her determination of this issue is entitled to deference in the absence of legal error or palpable and overriding error of fact.

33 CPL submits that the GSA compromises its rights and claims, and thus, challenges the express finding of the supervising judge that the settlement neither compromises the rights of creditors before it, nor deprives them of their existing contractual rights. The applicant relies upon the following effects of the GSA in making this submission:

> (i) a priority payment of $75 million out of the proceeds of the sale of bonds owned by Calpine Canada Resources Company;
>
> (ii) the release of a potential claim against Calpine Canada Energy Limited, the parent of Calpine Canada Resources Company, which is a partner of Calpine Energy Services Canada Ltd., against which CPL has a claim;
>
> (iii) the dismissal of a claim by Calpine Canada Energy Limited against Quintana Canada Holdings LLC, thereby depleting Calpine Canada Energy Limited of a potential asset which that company could use to satisfy any potential claim by CPL for any shortfall, were it not for the release of claims against Calpine Canada Energy Limited (see (ii) above); and
>
> (iv) the dismissal of the Greenfield Action brought by another CCAA Debtor against Calpine Energy Services Canada Ltd. for an alleged fraudulent conversion of its interest in Greenfield LP which was developing a 1005 Megawatt generation plant.

34 For purposes of the CCAA proceedings, the applicant is a creditor of Calpine Energy Services Canada Ltd., Calpine Canada Power Ltd. and perhaps, also, Calpine Canada Resources Company. The GSA does not change its status as a creditor of those companies, nor does it bar the applicant from any existing claims against those companies.

35 In my view, the submission of the applicant does not show any palpable and overriding error in the findings of the supervising judge that the right of creditors not parties to the GSA have not been compromised or taken away. Firstly, there is no compromise of debt if such indebtedness, as ultimately found due to the applicant, is paid in full, which is the likely result as found by the supervising judge, albeit she acknowledged that this result was not guaranteed (Reasons, para. 81). Secondly, and in any event, the fact that the GSA impacts upon the assets of the debtor companies, against which the applicant may ultimately have a claim for any shortfall experienced by it, is a common feature of any settlement agreement and as earlier explained, does not automatically result in a vote by the creditors. The further fact that one of the affected assets of the debtor companies is a cause of action, or perhaps, more correctly, a possible cause of action, does not abrogate the rights of a creditor albeit there may be less monies to be realized at the end of the day.

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36 The GSA does not usurp the right of the creditors to vote on a plan of arrangement if it becomes necessary to propose such a plan to the creditors. As explained by the supervising judge, the settlement between the CCAA Debtors and the US Debtors unlocked the Canadian proceedings to meaningful progress in asset realization and claims resolution, and provided the mechanisms for resolving the remaining issues and significant creditor claims, and the clarification of priorities.

37 It is correct, of course, that if the claims of CPL are paid in full in the course of the CCAA proceedings, it will never be necessary for it to vote on a plan of arrangement. The applicant should have no complaint with that result. On the other hand, if the claims are not satisfied, it seems likely a plan of arrangement will ultimately be proposed to the applicant, who will then have its right to vote on any such plan.

38 CPL argues that the supervising judge was not entitled to assess the merits of the GSA *vis-à-vis* the creditors as this was a matter for the exclusive business judgment of the creditors and to be exercised by their vote. As became apparent during the course of its submissions, if a vote were required, from the perspective of the CPL, this would give it veto power over the GSA. Unless clearly mandated by the statute, this is a result to be avoided. While it is understandable that an individual creditor seeks to obtain as much leverage as possible in order to enhance its negotiating position, the objectives and purposes of the CCAA could easily be frustrated in such circumstances by the self interest of a single creditor. Court approval requires, as a primary consideration, the determination that an agreement is fair and reasonable and will be beneficial to the debtor and its stakeholders generally. As the supervising judge noted, court approval of settlements and major transaction can and often is given over the objections of one or more parties because the court must act for the greater good consistent with the purpose and spirit and within the confines of the legislation.

39 I am not persuaded that the applicant has demonstrated any reasonably arguable error of law in the reasons of the supervising judge or any palpable and overriding errors in her findings of fact or findings of mixed fact and law. In the absence of any such error, it follows that she had discretion to approve the GSA, which she exercised based upon her assessment of the merits and reasonableness of the settlement, and other factors in accordance with the principles set out in the authorities, cited in her reasons, governing the approval of transactions, including settlements, during the stay period prior to a plan of arrangement being submitted to the creditors.

Conclusion

40 CPL has failed to establish serious and arguable grounds for granting leave. In particular, two of the factors used to assess whether this criterion is present have not been met. It has not been demonstrated that the point on appeal is of significance to the parties having regard to the fact dependent nature of whether a plan of arrangement has been proposed to creditors. More importantly, having regard to the standard of review and the findings of the supervising judge, the applicant has not demonstrated that the appeal for which leave is sought is *prima facie* meritorious.

41 The application for leave is dismissed. It follows that the application for a stay likewise fails and is dismissed.

42 Finally, I would be remiss if I did not acknowledge the excellent quality of the submissions, both written and oral, of counsel on these applications. The submissions were of great assistance in permitting the application to be dealt with in an abbreviated time frame.

Application dismissed.

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TAB 3

2012 BCSC 1773
British Columbia Supreme Court [In Chambers]

Great Basin Gold Ltd., Re

2012 CarswellBC 3710, 2012 BCSC 1773, [2013] B.C.W.L.D. 1881, 224 A.C.W.S. (3d) 22, 99 C.B.R. (5th) 219

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36

In the Matter of the Business Corporations Act, S.B.C. 2002, c. 57

In the Matter of Great Basin Gold Ltd. Petitioner

Fitzpatrick J.

Heard: November 20, 2012
Oral reasons: November 20, 2012
Docket: Vancouver S126583

Counsel: P.J. Reardon, J. Cockbill for Petitioner
J.R. Sandrelli, C. Cheuk for Certain Unaffiliated Holders of the Petitioner's Senior Unsecured Convertible Debentures (the "Noteholders")
P. Rubin for Credit Suisse, AG
J.I. McLean, Q.C. for Monitor, KPMG Inc.

Subject: Insolvency; Income Tax (Federal)

APPLICATION by debenture holders of insolvent corporation for order implementing settlement agreement with one of corporation's creditors.

Fitzpatrick J., **In chambers:**

1 Much of the history of this *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*") proceeding is outlined in my earlier reasons: *Great Basin Gold Ltd., Re*, 2012 BCSC 1459 (B.C. S.C.).

2 Broadly speaking, there were substantial issues joined between the principal combatants, Credit Suisse and the Ad Hoc Group, as defined in those reasons. Those issues principally related to the approval of the DIP loan facility that I had earlier granted in favour of Credit Suisse. The Ad Hoc Group disputed the granting of that DIP facility and launched an appeal of my October 1 order. I also understand that certain proceedings were commenced in the United States by the Ad Hoc Group towards a challenge of the granting of the guarantee and security by the U.S. companies of the group.

3 Following the issuance of those reasons on October 1, 2012, Credit Suisse and the Ad Hoc Group arrived at a tentative settlement of the issues arising between them. On October 16, 2012, I granted an order authorizing the petitioner to enter into this settlement agreement. The order also provided that the petitioner and the trustee under the trust indenture, Computershare Trust Company of Canada, were authorized to enter into such agreements as are required by the terms of the settlement. The members of the Ad Hoc Group are participants under the trust indenture.

4 An important aspect of the settlement negotiated by the Ad Hoc Group for the benefit of the entire debentureholders group is a guarantee from the U.S. holding company, Great Basin Gold Inc. ("GBGI"), and also certain subordinate security issued by GBGI in relation to that guarantee. From the debentureholder group's perspective, this settlement results in a substantial improvement of their current position. As with most settlement agreements, in return for these benefits, the debentureholder group must give up certain things. The agreements also provide that the debentureholder

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group will not proceed with certain challenges asserted to date, that being principally relating to the Credit Suisse guarantee and security that was approved by my earlier orders. The debentureholder group must also abandon the appeal proceedings and the U.S. proceedings which are referred to above. Finally, the debentureholder group must also agree to abandon the criminal interest rate issue, and other challenges to such matters as the KERP and the appointment of CIBC World Markets as the financial advisor.

5 Understandably, Credit Suisse requires that any settlement be approved by the entire debentureholders group and they also require an opinion from a lawyer to the effect that the documentation to evidence the settlement, including an intercreditor agreement, is binding upon the entire debentureholder group.

6 The significance of the settlement is that it buys peace between Credit Suisse and the Ad Hoc Group. At the present time, the Credit Suisse DIP facility is in default and further funding under the DIP facility is in limbo pending a finalization of the settlement. Accordingly, the finalization of the settlement is of tremendous significance in this case such that it will allow a continuation of the DIP financing to be advanced to the GBG Group who is desperately in need of these funds.

7 The difficulty that arises in terms of finalizing the settlement relates to how the parties can ensure that the entire debentureholder group will be bound by the settlement. The trust indenture does provide for the calling of meetings to consider resolutions by the debentureholder group. However, counsel for the Ad Hoc Group candidly points out that the full extent of what is intended to be agreed to by the debentureholder group under the settlement may not be within the specific terms of resolutions contemplated by the trust debenture.

8 In any event, I note that with respect to some matters at least, the trust indenture does provide for a meeting process by which a meeting may be held and written resolutions would be voted upon. I am also advised that those matters would require a special resolution, or in other words, a two-thirds majority.

9 It is of some significance on this application that the Ad Hoc Group, together with another debentureholder who is also in support of this application, hold in excess of a two-thirds majority from among the overall debentureholder group.

10 I am advised that it is not possible in the circumstances to even call a meeting that the debentureholders under the trust indenture given the exigencies of the situation in relation to the need for funding. Nevertheless, there has been some effort to engage the trustee under the trust indenture, Computershare. There have been ongoing discussions between the Ad Hoc Group and Computershare in that the trustee has been kept apprised of the settlement negotiations and the terms of the tentative settlement. I am advised that Computershare is fully supportive of the settlement and has no difficulty, subject to these issues relating to process, in proceeding with these transactions.

11 There have also been efforts to engage other debentureholders who are not represented by the Ad Hoc Group and the other debentureholder who supports the application. Following my earlier order on October 16, Computershare forwarded to the debentureholders copies of certain pleadings relating to this transaction which reference the terms of the proposed settlement. I am also advised by counsel for the Ad Hoc Group that their offices have fielded a number of calls from these other debentureholders. So it cannot be said that the other debentureholders are entirely in the dark in terms of what has been tentatively agreed to by the Ad Hoc Group and what is intended to be accomplished through the settlement agreement.

12 The issue in the first instance is whether I have the jurisdiction to provide the relief granted. The relief sought is not only an approval of the settlement agreement, but also an order authorizing the trustee, Computershare, to execute the various documents related to the settlement agreement such that these documents will be legal, valid and binding obligations of the trustee and all debentureholders.

13 The applicable statutory authority is s. 11 of the *CCAA* which endows the court with a wide statutory discretion to grant such orders as are "appropriate in the circumstances":

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General power of court

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.

14 As discussed by the Supreme Court of Canada in *Ted Leroy Trucking Ltd., Re*, 2010 SCC 60 (S.C.C.), the *CCAA* is a remedial statute and the court has "broad and flexible authority" to facilitate the reorganization of the debtor towards achieving the objectives of the *CCAA*, including avoiding the social and economic losses arising from restructuring proceedings: paras. 15-19. The exercise of the court's discretion was further discussed by the Court at paras. 59-72. In particular, the Court stated:

[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.

15 The last paragraph of the above quote makes the point that the chances of achieving a successful restructuring proceeding increase where the parties can agree on certain issues. Settlement agreements between the parties in these types of proceedings are very much encouraged where resolutions take place in the boardroom, as opposed to the courtroom. There is every reason to encourage such settlements, with approval and implementation subject to appropriate judicial oversight.

16 There is ample authority to the effect that s. 11 of the CCAA provides the court with jurisdiction to approve settlements even before the presentation of a plan of arrangement: *Calpine Canada Energy Ltd., Re*, 2007 ABCA 266 (Alta. C.A. [In Chambers]) at para. 26, *Nortel Networks Corp., Re*, 2010 ONSC 1708 (Ont. S.C.J. [Commercial List]) at para. 71.

17 In *Nortel Networks*, Mr. Justice Morawetz sets out the test to be applied in approving a settlement agreement:

[73] A Settlement Agreement can be approved if it is consistent with the spirit and purpose of the CCAA and is fair and reasonable in all circumstances. What makes a settlement agreement fair and reasonable is its balancing of the interests of all parties; its equitable treatment of the parries, including creditors who are not signatories to a settlement agreement; and its benefit to the Applicant and its stakeholders generally.

18 I have no difficulty in concluding that the settlement agreement between Credit Suisse, the Ad Hoc Group and the petitioner group is fair and reasonable in the circumstances. The crux of the issue here is whether it is fair and reasonable to those debentureholders who have not yet participated in this process and have not perhaps fully appreciated the import of the agreement, particularly as it relates to the benefits to be achieved by the debentureholder group and the rights that the group will be giving up as a result of the transactions.

19 I would emphasize again this settlement has arisen by extensive negotiations as between Credit Suisse and the Ad Hoc Group. While those negotiations have taken place on the part of the Ad Hoc Group towards its own interests, inevitably the gains will accrue to the debentureholder group as a whole. Having considered the terms of the overall settlement agreement, I would be astounded if any debentureholders who were fully aware of those matters were to

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take a contrary position towards opposing the settlement agreement. Again, it is of significance that as a result of this settlement, funding under the DIP facility will continue, which will be a benefit to all stakeholders.

20 Nevertheless, I agree that fairness and reasonableness dictate in these proceedings that those other debentureholders have some input. The process already undertaken by the Ad Hoc Group has addressed that matter to a certain extent. What is proposed is that a more fullsome notice of the settlement agreement be given to the debentureholder group as a whole.

21 Firstly, it is proposed that there be a press release which will include reference to not only the pleadings but the specific settlement documents which are posted on the Monitor's website. In addition, the press release will refer to counsel for the Ad Hoc Group, in Canada, the U.S. and South Africa, who are available to respond to any enquiries from debentureholders regarding the settlement agreement. Secondly, Computershare is to request that CDS send a notice to the debentureholders of the order sought today (called the "Settlement Implementation Order"). That notice will, as will the press release, highlight to the debentureholders that the deadline for any debentureholder to apply to vary, rescind or otherwise object to the Settlement Implementation Order will be within 21 days of the date of the Order. If there is no objection with that 21-day period, the settlement agreement will be fully effective and will constitute legal, valid and binding obligations of Computershare and all of the debentureholders and the consequences of not applying to challenge this Order will also be brought specifically to the attention of those persons reading the press release and the notice.

22 The Monitor had earlier indicated its support of the settlement agreement in accordance with the Third Report which was considered on the earlier application. Counsel for the Monitor has again confirmed its support of the settlement agreement and the process by which notice is to be given to the other debentureholders outlined above. Not surprisingly, the GBG Group is also in support.

23 I am satisfied that this process is appropriate and will give any other debentureholder sufficient time to challenge the Order if they wish. Again, I would emphasize that it is a critical aspect of this restructuring that this settlement be put in place as soon as possible so that the funding for the restructuring can proceed. It has already been stalled to some extent and no doubt to the detriment of the stakeholders as a whole. It is time to put an end to this prejudice delay and more the restructuring forward. Accordingly, the order sought is granted.

Application granted.

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TAB 4

2017 BCSC 1968
British Columbia Supreme Court

Walter Energy Canada Holdings, Inc. (Re)

2017 CarswellBC 3037, 2017 BCSC 1968, [2017] B.C.W.L.D. 6712,
[2017] B.C.W.L.D. 6713, 284 A.C.W.S. (3d) 688, 54 C.B.R. (6th) 57

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, as Amended

And In the Matter of a Plan of Compromise and Arrangement of New Walter Energy Canada Holdings, Inc., New Walter Canadian Coal Corp., New Brule Coal Corp., New Willow Creek Coal Corp., New Energybuild Holdings ULC

Fitzpatrick J.

Heard: October 6, 2017
Judgment: November 1, 2017
Docket: Vancouver S1510120

Counsel: P. Riesterer, for Petitioners
T. Jeffries, for United Mine Workers of America 1974 Pension Plan and Trust
M. Nied, for Warrior Met Coal, LLC
J. Sanders, for United Steelworkers, Local 1-424
V. Tickle, P.J. Reardon, for Monitor, KPMG

Subject: Civil Practice and Procedure; Insolvency

APPLICATION by respondent for approval of settlement of appeal.

Fitzpatrick J.:

Introduction

1 The petitioners, now called the New Walter Canada Group, apply for an order approving a settlement of certain claims. This is a significant development in these *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 (the "*CCAA*") proceedings, in that the settlement will pave the way so as to allow all other claims to be settled expeditiously. Importantly, it will also allow the distribution of substantial funds to the creditors arising from the earlier monetization of the majority of the assets.

2 The petitioners also seek authorization to advance further funds to the U.K. arm of the Walter Energy group of companies, and specifically, Energybuild Group Limited or Energybuild Ltd. ("Energybuild"), on a secured basis and not exceeding an aggregate amount of 900,000. Finally, the petitioners seek an extension of the stay period to December 15, 2017.

3 For the reasons that follow, I grant the relief sought by the petitioners.

Background

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4 The history of this matter has already been recounted in numerous decisions of this Court: *Walter Energy Canada Holdings, Inc., Re*, 2016 BCSC 1413 (B.C. S.C.) ; 2016 BCSC 2470 (B.C. S.C.); 2017 BCSC 53 (B.C. S.C.). Essentially, the coal mining assets of the petitioners were sold and the focus of the proceeding then moved to a consideration of the claims advanced by creditors, or alleged creditors.

5 The amounts available for distribution to the creditors is estimated to be in excess of $63 million by the end of 2017.

6 The most significant claim advanced against the petitioners was that of a U.S. entity, the United Mine Workers of America 1974 Pension Plan and Trust (the "1974 Plan"). The 1974 Plan asserted its claim pursuant to certain "controlled group" provisions of U.S. legislation, being the *Employee Retirement Income Security Act of 1974*, 29 U.S.C.]§ 1001, as amended ("*ERISA*"). The significance of the 1974 Plan's claim cannot be understated as it was in excess of $1.2 billion. If the claim was valid, it stood to consume the majority of the funds available for distribution to the other creditors, such that the substantial Canadian creditors' claims would have received only a nominal recovery.

7 The validity of the 1974 Plan's claim was addressed by this Court. On May 1, 2017, I held that the 1974 Plan's claim was governed by Canadian substantive law and not U.S. substantive law: *Walter Energy Canada Holdings, Inc., Re*, 2017 BCSC 709 (B.C. S.C.) at paras. 177-78, 182. Effectively, this resulted in the rejection of the 1974 Plan's claim against the petitioners.

8 The 1974 Plan filed an application for leave to appeal from my decision. Leave was granted by the British Columbia Court of Appeal on June 9, 2017. The appeal was scheduled to be heard on August 16, 2017. Eventually, the hearing date was adjourned in light of the ongoing negotiations between the parties which, if successful, would obviate the need to proceed.

9 In late September 2017, those negotiations were successful and resulted in the preparation of the Settlement Term Sheet Re Plan of Compromise and Arrangement (the "Settlement Term Sheet") which is presented for approval on this application.

10 There is no opposition to the approval of the Settlement Term Sheet. All stakeholders appearing are in support. The evidence on this application includes the affidavit #15 of William Aziz of BlueTree Advisors Inc., the Chief Restructuring Officer, and the Monitor who has filed its Thirteenth Report dated October 4, 2017.

The Settlement Term Sheet

11 As described above, the Settlement Term Sheet is the result of lengthy arm's length negotiation between the petitioners, the 1974 Plan and Warrior Met Coal, LLC ("Warrior"). Warrior is another U.S. entity who had advanced claims against some of the petitioners' assets. Warrior's claim was significant because, if the 1974 Plan's claim was not valid, the full amount of the claims against the operating subsidiaries within the New Walter Canada Group would be paid in full, resulting in monies flowing to the holding companies within the New Walter Canada Group against which Warrior's claim had been filed.

12 The essential terms of the Settlement Term Sheet are as follows.

a) Settlement of Warrior's Claims

13 The Settlement Term Sheet provides for a settlement and allowance of two claims asserted by Warrior: (i) a claim in respect of certain shared services provided by the U.S. Walter Energy entities to the Canadian Walter Energy entities (the "Shared Services Claim"); and (ii) a claim in relation to accrued but unpaid interest owing in respect of a promissory note between Walter Energy, Inc. and Walter Energy Canada Holdings, Inc. dated April 1, 2011 and related documents, which claim was compromised pursuant to an order of the Court pronounced December 21, 2016. That compromise was made pursuant to a proposal by the original Canadian Walter Energy entities pursuant to the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, which proposal was approved by the Court on December 21, 2016 (the "Hybrid Debt Claim").

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14 Under the Settlement Term Sheet, Warrior's claims will be an Allowed Claim, as that phrase is defined in a Claims Process Order granted in these proceedings on August 16, 2016. Warrior's claims will be as follows: the Shared Services Claim will be an Allowed Claim in the amount of $9,892,193.32; and, the Hybrid Debt Claim will be an Allowed Claim to be further compromised such that it is equal to the amount of the Available Net Proceeds (as described below). Further, in the Settlement Term Sheet, Warrior expressly consents to the use of the Available Net Proceeds in the manner described below.

b) Settlement of the 1974 Plan's Claim, Appeal and Related Cost Awards

15 The Settlement Term Sheet provides that, in consideration of the 1974 Plan abandoning its appeal, the petitioners will pay the first $13 million of Available Net Proceeds to the 1974 Plan, and Warrior shall receive the remainder (if any) of Available Net Proceeds (after the payment of certain other amounts described below) in respect of the Hybrid Debt Claim.

16 Further, the petitioners have agreed that, in consideration of the abandonment of the 1974 Plan's appeal, they will (i) not pursue costs against the 1974 Plan in relation to proceedings arising from the assertion of its claim, both in this Court and in the Court of Appeal; and (ii) pay the costs of the United Steelworkers Local 1-424 ("USW"). The USW had been very much involved in opposing the efforts of the 1974 Plan to assert its claim. The USW's costs are fixed at $75,000, which is to be paid from the funds available for distribution.

17 The 1974 Plan's agreement to abandon its appeal is contingent upon the petitioners' payment of $13 million to the 1974 Plan from the Available Net Proceeds. The uncertainty as to whether this payment can be made arises because it is not yet known exactly what claims might be advanced against the petitioners.

18 The process under the Claims Process Order has been underway for some time now. Arising from that process, there are Allowed Claims of $23.8 million and unresolved claims of $7.5 million. However, more recently, the Monitor has been undertaking the process of flushing out any further restructuring claims pursuant to the Claims Process Amendment Order granted August 15, 2017. No claims have yet been received, however, the claims bar date is at the end of today. As of the hearing, no claims had been received that would potentially result in less than $13 million being available to be paid to the 1974 Plan from the Available Net Proceeds.

19 Accordingly, the 1974 Plan will adjourn its appeal so as to conclude the unresolved restructuring claims process towards determining that $13 million will, in any event, be available to be paid to the 1974 Plan, rather than Warrior, after deducting (i) all payments and taking all reserves required to administer and wind down the estate as contemplated; (ii) payment of the USW costs amount; and (iii) payment in full of all Allowed Claims, including the Shared Services Claim but excluding the Hybrid Debt Claim (the "Available Net Proceeds"). The 1974 Plan will then abandon its appeal following the petitioners' payment to the 1974 Plan of $13 million.

20 In the event that additional claims are filed in the unresolved restructuring claims process and they become Allowed Claims, such that it is determined that the Available Net Proceeds will be insufficient to pay $13 million to the 1974 Plan, the Settlement Term Sheet provides that (i) the 1974 Plan may bring its appeal at that time; and (ii) the petitioners, the Monitor and the USW may pursue costs against the 1974 Plan in relation to proceedings arising from the assertion of its claim, both in this Court and in the Court of Appeal.

21 Under the Settlement Term Sheet, the 1974 Plan's claim shall not become an Allowed Claim unless the 1974 Plan brings forward its appeal in the manner permitted by the Settlement Term Sheet and a final order is issued declaring that the 1974 Plan's claim is an Allowed Claim in respect of the petitioners.

22 The Settlement Term Sheet also provides that the director of the corporations composing the petitioners (who was also the director of the original Canadian Walter Energy petitioner companies) shall be paid an aggregate amount

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of US$250,000 from the Available Net Proceeds "in consideration for his commitment to [the petitioners] throughout the *CCAA* [p]roceedings".

c) Plan of Compromise or Arrangement

23 Upon the completion of the unresolved restructuring claim process or such earlier date as the petitioners and the Monitor may decide (after consultation with Warrior), the petitioners intend to bring forward a motion seeking the Court's approval of a plan of compromise or arrangement (the "Plan") that contains the principal terms set out in the Settlement Term Sheet. I am advised that the petitioners will bring this motion only if they and the Monitor are satisfied that sufficient funds will be available to address all remaining matters in the *CCAA* proceedings and the orderly wind-down or other process for the Walter U.K. Group, which includes Energybuild.

24 The terms that will be included in the proposed Plan are set out in the Settlement Term Sheet and include, among others terms, the following:

a) Warrior, as the sole claimant with a claim that is to be compromised under the Plan, shall be the sole claimant entitled to vote on the Plan;

b) the Plan will provide for the payment in full in cash of all claims that become Allowed Claims other than the Hybrid Debt Claim, provided that the petitioners and the Monitor determine that:

i. the petitioners have an amount sufficient to pay in full in cash all Allowed Claims and the full amount of all Claims that become Allowed Claims after the date of the Settlement Term Sheet;

ii. if there is an interim distribution, the petitioners have an amount sufficient to pay in full in cash any claim that is the subject of an unresolved Notice of Dispute if all such disputed claims were to become Allowed Claims; and

iii. the petitioners have retained an amount sufficient to address professional fees and other costs necessary for the effective administration of all remaining matters in connection with these *CCAA* proceedings, and to address whatever process occurs with respect to the Walter U.K. Group.

25 The 1974 Plan has agreed to support the petitioners in obtaining Court approval and implementation of the Plan.

d) Release of Claims against the Walter U.K. Group

26 Cambrian Energybuild Holdings ULC ("Cambrian") is one of the petitioners. It is the holding company for the coal mining operating companies in the United Kingdom. Its subsidiaries include Energybuild, the operating entity or entities that own and operate the Aberpergym underground coal mine located at the Neath Valley in Wales. The mine is currently in care and maintenance.

27 Efforts have been underway for some time on the part of the petitioners and the directors of the Walter U.K. Group in analyzing Energybuild's business and seeking opportunities to sell Energybuild and its affiliates or their assets. An interested party has come forward regarding a potential sale of Energybuild and certain of its affiliates. The interested party remains interested in acquiring these assets, but has requested that certain conditions be satisfied in respect of claims that may be made against Energybuild and any of its affiliates that may be acquired. One of those potential claims is that of the 1974 Plan, who similarly asserts that the Walter U.K. Group entities are liable for its claim under *ERISA*. In addition, there appears to be the potential for Warrior to assert claims directly against the Walter U.K. Group entities in relation to its intercompany claims by the U.S. Walter Energy entities.

28 Therefore, the petitioners and the Walter U.K. Group have sought, as part of the Settlement Term Sheet, to address any such claims. If not addressed, these lingering issues may result in the interested party disengaging entirely from the negotiations which the stakeholders hoped would lead to a sale of Energybuild and its assets.

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29 The Settlement Term Sheet addresses the principal conditions precedent that relate to the sale of Energybuild and certain of its affiliates. In order to facilitate the sale of the Walter U.K. Group, any entity included within that Group or any of their respective assets, the Settlement Term Sheet provides for releases by both the 1974 Plan and Warrior on certain terms. These releases are effective immediately and are not dependent on whether there is at least Available Net Proceeds of $13 million available for payment to the 1974 Plan or that the appeal is abandoned. Accordingly, these releases allow the petitioners and the directors of the Walter U.K. Group to proceed immediately to conclude a sale in the U.K., if possible.

30 The Term Sheet provides that the proceeds from any sale of the U.K. assets are to be applied as follows:

a) first, to repay amounts advanced to or for the benefit of the Walter U.K. Group on a secured basis, as has already been authorized by orders granted in these *CCAA* proceedings. To date, 600,000 has been advanced and it is proposed that authorization be given for a further 300,000;

b) second, to wind up any Walter U.K. Group entity that is not the subject of any sale in a cost effective and tax efficient manner that protects the Walter U.K. Group's directors and officers from liability to the fullest extent possible, at the discretion of the petitioners;

c) third, if any amounts remain, such amounts shall be distributed to Warrior in respect of Warrior's claim asserted against the Walter U.K. Group, up to the maximum amount of 4,666,779; and

d) fourth, if any amounts remain, such amounts shall be distributed to Cambrian on account of its equity interest in Energybuild.

Approval of Settlement Term Sheet

31 The petitioners seek approval of the Settlement Term Sheet pursuant to the *CCAA*, s. 11, which provides that I may exercise my discretion to make any order that I consider "appropriate in the circumstances".

32 In *Great Basin Gold Ltd., Re*, 2012 BCSC 1773 (B.C. S.C. [In Chambers]) at para. 16, I concluded that s. 11 provides the necessary jurisdictional basis to consider and approve a settlement agreement even before the presentation of a plan of arrangement.

33 Regional Senior Justice Morawetz of the Superior Court of Justice has articulated, a number of times, the relevant considerations in approving a settlement in the *CCAA* context:

a. is the settlement fair and reasonable?

b. does the settlement provide substantial benefit to stakeholders? and

c. is the settlement consistent with the purpose and spirit of the *CCAA*?

See: *Labourers' Pension Fund of Central and Eastern Canada v. Sino-Forest Corp.*, 2013 ONSC 1078 (Ont. S.C.J. [Commercial List]) at para. 49, leave to appeal refused 2013 ONCA 456 (Ont. C.A.); *1511419 Ontario Inc., Re*, 2015 ONSC 7538 (Ont. S.C.J.) at para. 14.

34 In my view, all three of the above considerations are satisfied here and support that the Settlement Term Sheet should be approved:

a) the settlement removes a major stumbling block in providing a distribution to creditors, many of whom are former employees of the petitioners who have suffered financial distress as a result of not being paid their wages and other benefits;

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b) if the 1974 Plan's claim were to proceed to a hearing of the appeal, there would be significant delay in resolving the issues. In addition, there would be significant cost to the petitioners, the CRO and the Monitor in participating in those proceedings;

c) the settlement avoids the risk of the 1974 Plan being successful, a result that would effectively deprive the claimants with Allowed Claims of any meaningful recovery;

d) the settlement allows the petitioners to proceed to a determination of the remaining claims on their merits which will also facilitate a final distribution to the creditors;

e) all of the Allowed Claims, many of whom are former employees, will receive their claim amounts in full. Only Warrior will face any compromise of its claim. Effectively, the payment of $13 million to the 1974 Plan has no effect on the Allowed Claims since it is sourced from the Available Net Proceeds that would otherwise be paid to Warrior; and

f) the settlement will also facilitate the sale of the Walter U.K. Group assets in terms of the releases from the 1974 Plan and Warrior, which are effective immediately. A timely resolution of that aspect of the restructuring will be to the benefit of all parties in bringing these proceedings to a close.

35 There can be no doubt but that this settlement achieves what few *CCAA* proceedings achieve, namely a somewhat timely but full recovery for the vast majority of claimants. That the parties were able to resolve their differences to avoid the complex and costly legal battles to come is a testament to the ingenuity of the stakeholders and the flexibility that the *CCAA* affords in these difficult circumstances.

36 In *Ted Leroy Trucking Ltd., Re*, 2010 SCC 60 (S.C.C.) , the Court confirmed the well-known description of the *CCAA* as being a remedial statute and that the court has "broad and flexible authority" to facilitate the reorganization of the debtor towards achieving the objectives of the *CCAA*, including avoiding the social and economic losses arising from restructuring proceedings: paras. 15-19.

37 These particular comments of the Court in *Century Services* bear repeating in respect of this application:

[70] . . . 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.

[Emphasis added.]

38 The Monitor supports the approval of the Settlement Term Sheet as being fair and reasonable, describing it as a "highly favourable outcome" for the petitioners' creditors who are to be paid in full. The Monitor expects that there will be sufficient funds to pay all of the Allowed Claims such that there is little likelihood of there being insufficient funds with which to pay $13 million to the 1974 Plan. In the circumstances, this appears to be a reasonable expectation.

39 The only hesitation I had with respect to the approval of the Settlement Term Sheet arose from the proposal that the director be paid US$250,000, in light of what was described as his commitment and the risks that he has undertaken in the fulfillment of his duties throughout these proceedings.

40 A somewhat similar circumstance arose in *Veris Gold Corp., Re*, 2015 BCSC 399 (B.C. S.C.) , where approval of fees was sought in relation to amounts said to have accrued throughout a *CCAA* proceeding. In that case, the approval of the fees would have affected pre-existing claims after the fact:

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[62] The matter of timing requires some discussion. The effect of the relief now sought by the Special Committee is such that their fees would be paid in priority to DB's security. WBox takes no position in respect of the relief sought, no doubt given the higher priority of its security as against DB's secured position.

[63] If such an application had been brought in a more timely manner, then the court would have been in a position to consider the matter based on the circumstances at the time. In addition, the stakeholders, such as DB, would have been able to assess the relief sought in respect of its position at that time. Court-ordered charges to protect persons providing services to the debtor can be sought under the *CCAA*: see for example, s. 11.4 (critical suppliers); s. 11.52 (fees and expenses of financial, legal and other experts).

[64] This is not unlike a situation where court-ordered charges are sought when services have already been provided and relief is only sought some time later. Inevitably, the argument is that it is only "fair" that the services delivered prior to the date of the charge be included. In addition, this is not unlike the situation where limits of spending have been imposed in respect of such charges, and the limits are exceeded and only later sought to be increased. In all of these circumstances, delay in seeking relief disadvantages the stakeholders in terms of considering the effect of the relief sought in the context of the current situation, and deprives them of a consideration of other options that might be available at the time. In addition, this delay puts the court in the very uncomfortable position of potentially depriving persons who have provided such services in good faith of the normal costs of doing so.

[Emphasis added.]

41 Having considered the matter, I do not see that any similar issues or disadvantages to the stakeholders arise in relation to the proposed payment to be made to the director. Unlike the situation in *Veris Gold*, this amount to be paid is only sourced from the Available Net Proceeds, which effectively means that Warrior will fund that amount from funds that would otherwise be paid to it. Warrior agrees to the payment of that amount. Accordingly, no Allowed Claims will be affected.

42 I conclude that the Settlement Term Sheet is fair and reasonable, that it provides a substantial benefit to the creditors of the petitioners and that it is consistent with the purpose and spirit of the *CCAA*.

Approval of Further Advances to the Walter U.K. Group

43 As set out above, the petitioners have already been funding the Walter U.K. Group in respect of its working capital requirements. The advances, which are secured, are currently outstanding in the amount of 600,000.

44 Mr. Aziz indicates that, with the releases set out in the Settlement Term Sheet now in hand, further time will be needed to hopefully conclude the negotiations with the party who has expressed an interest in purchasing the Walter U.K. Group's assets. The petitioners have been provided with cash flow forecasts for Energybuild that indicate a cash need of approximately 300,000 through to the end of the proposed extended stay period, namely December 15, 2017.

45 As such, the New Walter Canada Group is seeking this Court's authorization to advance up to an additional 300,000 (for an aggregate maximum of 900,000) on a secured basis to the Walter U.K. Group to fund Energybuild's working capital needs while negotiations regarding a potential sale continue. Mr. Aziz advises that no additional funds will be advanced unless the petitioners determine that such further advance will be in the best interests of Cambrian and the other members of the petitioners. By that statement, I take it to be the case that, if the negotiations do not result fairly quickly in a sale of the assets, other measures will be considered to deal with the Walter U.K. Assets as expeditiously and efficiently as possible.

46 All of the circumstances here support the conclusion that the further interim financing should be approved based on the factors set out in the *CCAA*, s. 11.2(4). That financing is approved on the terms sought.

Stay Extension

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47 The current stay period expires today, October 6, 2017.

48 The petitioners seek an extension of the stay period to December 15, 2017. This extension is being requested to allow them to complete the unresolved restructuring claims process; possibly bring court proceedings to address any disputed claims; sell the Walter U.K. Group assets, if possible; develop the Plan and bring it before the Court for approval to implement the Settlement Term Sheet; and finally, address the distribution of the proceeds.

49 Both Mr. Aziz and the Monitor confirm what is manifestly apparent; namely, that the petitioners continue to act in good faith and with due diligence in these proceedings. The Monitor supports the extension of the stay period as being a reasonable estimate of the time required to address these final matters.

50 I have no hesitation in concluding that the requested stay extension is appropriate in the circumstances and that the petitioners are acting in good faith and with due diligence: *CCAA*, s. 11.02(2) and (3).

Conclusion

51 The proposed settlement, as contained in the Settlement Term Sheet, is fair and reasonable. The Settlement Term Sheet, between the petitioners, Warrior and the 1974 Plan is approved. I also order that the parties to the Settlement Term Sheet comply with their obligations under the Settlement Term Sheet and that the Monitor assist in that respect by taking all reasonable and necessary steps to do so.

52 Cambrian Energybuild Holdings ULC is authorized to advance up to a further 300,000 (for an aggregate maximum of 900,000) to Energybuild, on a secured basis.

53 Finally, the stay of proceedings in respect of the petitioners is extended to December 15, 2017.

Application granted.

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TAB 5

2013 ONSC 1078
Ontario Superior Court of Justice [Commercial List]

Labourers' Pension Fund of Central and Eastern Canada v. Sino-Forest Corp.

2013 CarswellOnt 3361, 2013 ONSC 1078, 100 C.B.R. (5th) 30, 227 A.C.W.S. (3d) 930, 37 C.P.C. (7th) 135

In the Matter of the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as Amended

In the Matter of a Plan of Compromise or Arrangement of Sino-Forest Corporation, Applicant

The Trustees of the Labourers' Pension Fund of Central and Eastern Canada, The Trustees of the International Union of Operating Engineers Local 793 Pension Plan for Operating Engineers in Ontario, Sjunde Ap-Fonden, David Grant and Robert Wong, Plaintiffs and Sino-Forest Corporation, Ernst & Young LLP, BDO Limited (Formerly Known as BDO McCabe Lo Limited), Allen T.Y. Chan, W. Judson Martin, Kai Kit Poon, David J. Horsley, William E. Ardell, James P. Bowland, James M.E. Hyde, Edmund Mak, Simon Murray, Peter Wang, Garry J. West, Pöyry (Beijing) Consulting Company Limited, Credit Suisse Securities (Canada) In., TD Securities Inc., Dundee Securities Corporation, RBC Dominion Securities Inc., Scotia Capital Inc., CIBC World Markets Inc., Merrill Lunch Canada Inc., Canaccord Financial Ltd., Maison Placements Canada Inc., Credit Suisse Securities (USA) LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated (Successor by Merger to Banc of America Securities LLC), Defendants

Morawetz J.

Heard: February 4, 2013
Judgment: March 20, 2013
Docket: CV-12-9667-00CL, CV-11-431153-00CP

Counsel: Kenneth Rosenberg, Max Starnino, A. Dimitri Lascaris, Daniel Bach, Charles M. Wright, Jonathan Ptak, for Ad Hoc Committee of Purchasers including the Class Action Plaintiffs
Peter Griffin, Peter Osborne, Shara Roy, for Ernst & Young LLP, John Pirie and David Gadsden, for Pöyry (Beijing) Consulting Company Ltd.
Robert W. Staley for Sino-Forest Corporation
Won J. Kim, Michael C. Spencer, Megan B. McPhee for Objectors, Invesco Canada Ltd., Northwest & Ethical Investments LP and Comité Syndical National de Retraite Bâtirente Inc.
John Fabello Rebecca Wise, for Underwriters
Ken Dekker, Peter Greene for BDO Limited
Emily Cole, Joseph Marin for Allen Chan
James Doris for U.S. Class Action
Brandon Barnes for Kai Kit Poon
Robert Chadwick, Brendan O'Neill for Ad Hoc Committee of Noteholders
Derrick Tay, Cliff Prophet for Monitor, FTI Consulting Canada Inc.
Simon Bieber for David Horsley
James Grout for Ontario Securities Commission
Miles D. O'Reilly, Q.C. for Junior Objectors, Daniel Lam and Senthilvel Kanagaratnam

Subject: Insolvency; Civil Practice and Procedure; Corporate and Commercial; Securities

MOTION by representative plaintiffs for approval of settlement in class proceeding.

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Morawetz J.:

Introduction

1 The Ad Hoc Committee of Purchasers of the Applicant's Securities (the "Ad Hoc Securities Purchasers' Committee" or the "Applicant"), including the representative plaintiffs in the Ontario class action (collectively, the "Ontario Plaintiffs"), bring this motion for approval of a settlement and release of claims against Ernst & Young LLP [the "Ernst & Young Settlement", the "Ernst & Young Release", the "Ernst & Young Claims" and "Ernst & Young", as further defined in the Plan of Compromise and Reorganization of Sino-Forest Corporation ("SFC") dated December 3, 2012 (the "Plan")].

2 Approval of the Ernst & Young Settlement is opposed by Invesco Canada Limited ("Invesco"), Northwest and Ethical Investments L.P. ("Northwest"), Comité Syndical National de Retraite Bâtirente Inc. ("Bâtirente"), Matrix Asset Management Inc. ("Matrix"), Gestion Férique and Montrusco Bolton Investments Inc. ("Montrusco") (collectively, the "Objectors"). The Objectors particularly oppose the no-opt-out and full third-party release features of the Ernst & Young Settlement. The Objectors also oppose the motion for a representation order sought by the Ontario Plaintiffs, and move instead for appointment of the Objectors to represent the interests of all objectors to the Ernst & Young Settlement.

3 For the following reasons, I have determined that the Ernst & Young Settlement, together with the Ernst & Young Release, should be approved.

Facts

Class Action Proceedings

4 SFC is an integrated forest plantation operator and forest productions company, with most of its assets and the majority of its business operations located in the southern and eastern regions of the People's Republic of China. SFC's registered office is in Toronto, and its principal business office is in Hong Kong.

5 SFC's shares were publicly traded over the Toronto Stock Exchange. During the period from March 19, 2007 through June 2, 2011, SFC made three prospectus offerings of common shares. SFC also issued and had various notes (debt instruments) outstanding, which were offered to investors, by way of offering memoranda, between March 19, 2007 and June 2, 2011.

6 All of SFC's debt or equity public offerings have been underwritten. A total of 11 firms (the "Underwriters") acted as SFC's underwriters, and are named as defendants in the Ontario class action.

7 Since 2000, SFC has had two auditors: Ernst & Young, who acted as auditor from 2000 to 2004 and 2007 to 2012, and BDO Limited ("BDO"), who acted as auditor from 2005 to 2006. Ernst & Young and BDO are named as defendants in the Ontario class action.

8 Following a June 2, 2011 report issued by short-seller Muddy Waters LLC ("Muddy Waters"), SFC, and others, became embroiled in investigations and regulatory proceedings (with the Ontario Securities Commission (the "OSC"), the Hong Kong Securities and Futures Commission and the Royal Canadian Mounted Police) for allegedly engaging in a "complex fraudulent scheme". SFC concurrently became embroiled in multiple class action proceedings across Canada, including Ontario, Quebec and Saskatchewan (collectively, the "Canadian Actions"), and in New York (collectively with the Canadian Actions, the "Class Action Proceedings"), facing allegations that SFC, and others, misstated its financial results, misrepresented its timber rights, overstated the value of its assets and concealed material information about its business operations from investors, causing the collapse of an artificially inflated share price.

9 The Canadian Actions are comprised of two components: first, there is a shareholder claim, brought on behalf of SFC's current and former shareholders, seeking damages in the amount of $6.5 billion for general damages, $174.8

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million in connection with a prospectus issued in June 2007, $330 million in relation to a prospectus issued in June 2009, and $319.2 million in relation to a prospectus issued in December 2009; and second, there is a noteholder claim, brought on behalf of former holders of SFC's notes (the "Noteholders"), in the amount of approximately $1.8 billion. The noteholder claim asserts, among other things, damages for loss of value in the notes.

10 Two other class proceedings relating to SFC were subsequently commenced in Ontario: *Smith et al. v. Sino-Forest Corporation et al.*, which commenced on June 8, 2011; and *Northwest and Ethical Investments L.P. et al. v. Sino-Forest Corporation et al.*, which commenced on September 26, 2011.

11 In December 2011, there was a motion to determine which of the three actions in Ontario should be permitted to proceed and which should be stayed (the "Carriage Motion"). On January 6, 2012, Perell J. granted carriage to the Ontario Plaintiffs, appointed Siskinds LLP and Koskie Minsky LLP to prosecute the Ontario class action, and stayed the other class proceedings.

CCAA Proceedings

12 SFC obtained an initial order under the *Companies' Creditors Arrangement Act*, R.S.C. 1985, c. C-36 ("CCAA") on March 30, 2012 (the "Initial Order"), pursuant to which a stay of proceedings was granted in respect of SFC and certain of its subsidiaries. Pursuant to an order on May 8, 2012, the stay was extended to all defendants in the class actions, including Ernst & Young. Due to the stay, the certification and leave motions have yet to be heard.

13 Throughout the CCAA proceedings, SFC asserted that there could be no effective restructuring of SFC's business, and separation from the Canadian parent, if the claims asserted against SFC's subsidiaries arising out of, or connected to, claims against SFC remained outstanding.

14 In addition, SFC and FTI Consulting Canada Inc. (the "Monitor") continually advised that timing and delay were critical elements that would impact on maximization of the value of SFC's assets and stakeholder recovery.

15 On May 14, 2012, an order (the "Claims Procedure Order") was issued that approved a claims process developed by SFC, in consultation with the Monitor. In order to identify the nature and extent of the claims asserted against SFC's subsidiaries, the Claims Procedure Order required any claimant that had or intended to assert a right or claim against one or more of the subsidiaries, relating to a purported claim made against SFC, to so indicate on their proof of claim.

16 The Ad Hoc Securities Purchasers' Committee filed a proof of claim (encapsulating the approximately $7.3 billion shareholder claim and $1.8 billion noteholder claim) in the CCAA proceedings on behalf of all putative class members in the Ontario class action. The plaintiffs in the New York class action filed a proof of claim, but did not specify quantum of damages. Ernst & Young filed a proof of claim for damages and indemnification. The plaintiffs in the Saskatchewan class action did not file a proof of claim. A few shareholders filed proofs of claim separately. No proof of claim was filed by Kim Orr Barristers P.C. ("Kim Orr"), who represent the Objectors.

17 Prior to the commencement of the CCAA proceedings, the plaintiffs in the Canadian Actions settled with Pöyry (Beijing) Consulting Company Limited ("Pöyry") (the "Pöyry Settlement"), a forestry valuator that provided services to SFC. The class was defined as all persons and entities who acquired SFC's securities in Canada between March 19, 2007 to June 2, 2011, and all Canadian residents who acquired SFC securities outside of Canada during that same period (the "Pöyry Settlement Class").

18 The notice of hearing to approve the Pöyry Settlement advised the Pöyry Settlement Class that they may object to the proposed settlement. No objections were filed.

19 Perell J. and Émond J. approved the settlement and certified the Pöyry Settlement Class for settlement purposes. January 15, 2013 was fixed as the date by which members of the Pöyry Settlement Class, who wished to opt-out of either

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of the Canadian Actions, would have to file an opt-out form for the claims administrator, and they approved the form by which the right to optout was required to be exercised.

20 Notice of the certification and settlement was given in accordance with the certification orders of Perell J. and Émond J. The notice of certification states, in part, that:

> IF YOU CHOOSE TO OPT OUT OF THE CLASS, YOU WILL BE OPTING OUT OF THE ENTIRE PROCEEDING. THIS MEANS THAT YOU WILL BE UNABLE TO PARTICIPATE IN ANY FUTURE SETTLEMENT OR JUDGMENT REACHED WITH OR AGAINST THE REMAINING DEFENDANTS.

21 The opt-out made no provision for an opt-out on a conditional basis.

22 On June 26, 2012, SFC brought a motion for an order directing that claims against SFC that arose in connection with the ownership, purchase or sale of an equity interest in SFC, and related indemnity claims, were "equity claims" as defined in section 2 of the CCAA, including the claims by or on behalf of shareholders asserted in the Class Action Proceedings. The equity claims motion did not purport to deal with the component of the Class Action Proceedings relating to SFC's notes.

23 In reasons released July 27, 2012 [*Sino-Forest Corp., Re*, 2012 ONSC 4377 (Ont. S.C.J. [Commercial List])], I granted the relief sought by SFC (the "Equity Claims Decision"), finding that "the claims advanced in the shareholder claims are clearly equity claims". The Ad Hoc Securities Purchasers' Committee did not oppose the motion, and no issue was taken by any party with the court's determination that the shareholder claims against SFC were "equity claims". The Equity Claims Decision was subsequently affirmed by the Court of Appeal for Ontario on November 23, 2012 [*Sino-Forest Corp., Re*, 2012 ONCA 816 (Ont. C.A.)].

Ernst & Young Settlement

24 The Ernst & Young Settlement, and third party releases, was not mentioned in the early versions of the Plan. The initial creditors' meeting and vote on the Plan was scheduled to occur on November 29, 2012; when the Plan was amended on November 28, 2012, the creditors' meeting was adjourned to November 30, 2012.

25 On November 29, 2012, Ernst & Young's counsel and class counsel concluded the proposed Ernst & Young Settlement. The creditors' meeting was again adjourned, to December 3, 2012; on that date, a new Plan revision was released and the Ernst & Young Settlement was publicly announced. The Plan revision featured a new Article 11, reflecting the "framework" for the proposed Ernst & Young Settlement and for third-party releases for named third-party defendants as identified at that time as the Underwriters or in the future.

26 On December 3, 2012, a large majority of creditors approved the Plan. The Objectors note, however, that proxy materials were distributed weeks earlier and proxies were required to be submitted three days prior to the meeting and it is evident that creditors submitting proxies only had a pre-Article 11 version of the Plan. Further, no equity claimants, such as the Objectors, were entitled to vote on the Plan. On December 6, 2012, the Plan was further amended, adding Ernst & Young and BDO to Schedule A, thereby defining them as named third-party defendants.

27 Ultimately, the Ernst & Young Settlement provided for the payment by Ernst & Young of $117 million as a settlement fund, being the full monetary contribution by Ernst & Young to settle the Ernst & Young Claims; however, it remains subject to court approval in Ontario, and recognition in Quebec and the United States, and conditional, pursuant to Article 11.1 of the Plan, upon the following steps:

> (a) the granting of the sanction order sanctioning the Plan including the terms of the Ernst & Young Settlement and the Ernst & Young Release (which preclude any right to contribution or indemnity against Ernst & Young);
>
> (b) the issuance of the Settlement Trust Order;

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(c) the issuance of any other orders necessary to give effect to the Ernst & Young Settlement and the Ernst & Young Release, including the Chapter 15 Recognition Order;

(d) the fulfillment of all conditions precedent in the Ernst & Young Settlement; and

(e) all orders being final orders not subject to further appeal or challenge.

28 On December 6, 2012, Kim Orr filed a notice of appearance in the CCAA proceedings on behalf of three Objectors: Invesco, Northwest and Bâtirente. These Objectors opposed the sanctioning of the Plan, insofar as it included Article 11, during the Plan sanction hearing on December 7, 2012.

29 At the Plan sanction hearing, SFC's counsel made it clear that the Plan itself did not embody the Ernst & Young Settlement, and that the parties' request that the Plan be sanctioned did not also cover approval of the Ernst & Young Settlement. Moreover, according to the Plan and minutes of settlement, the Ernst & Young Settlement would not be consummated (*i.e.* money paid and releases effective) unless and until several conditions had been satisfied in the future.

30 The Plan was sanctioned on December 10, 2012 with Article 11. The Objectors take the position that the Funds' opposition was dismissed as premature and on the basis that nothing in the sanction order affected their rights.

31 On December 13, 2012, the court directed that its hearing on the Ernst & Young Settlement would take place on January 4, 2013, under both the CCAA and the *Class Proceedings Act, 1992*, S.O. 1992, c. 6 ("CPA"). Subsequently, the hearing was adjourned to February 4, 2013.

32 On January 15, 2013, the last day of the opt-out period established by orders of Perell J. and Émond J., six institutional investors represented by Kim Orr filed opt-out forms. These institutional investors are Northwest and Bâtirente, who were two of the three institutions represented by Kim Orr in the Carriage Motion, as well as Invesco, Matrix, Montrusco and Gestion Ferique (all of which are members of the Pöyry Settlement Class).

33 According to the opt-out forms, the Objectors held approximately 1.6% of SFC shares outstanding on June 30, 2011 (the day the Muddy Waters report was released). By way of contrast, Davis Selected Advisors and Paulson and Co., two of many institutional investors who support the Ernst & Young Settlement, controlled more than 25% of SFC's shares at this time. In addition, the total number of outstanding objectors constitutes approximately 0.24% of the 34,177 SFC beneficial shareholders as of April 29, 2011.

Law and Analysis

Court's Jurisdiction to Grant Requested Approval

34 The Claims Procedure Order of May 14, 2012, at paragraph 17, provides that any person that does not file a proof of claim in accordance with the order is barred from making or enforcing such claim as against any other person who could claim contribution or indemnity from the Applicant. This includes claims by the Objectors against Ernst & Young for which Ernst & Young could claim indemnity from SFC.

35 The Claims Procedure Order also provides that the Ontario Plaintiffs are authorized to file one proof of claim in respect of the substance of the matters set out in the Ontario class action, and that the Quebec Plaintiffs are similarly authorized to file one proof of claim in respect of the substance of the matters set out in the Quebec class action. The Objectors did not object to, or oppose, the Claims Procedure Order, either when it was sought or at any time thereafter. The Objectors did not file an independent proof of claim and, accordingly, the Canadian Claimants were authorized to and did file a proof of claim in the representative capacity in respect of the Objectors' claims.

36 The Ernst & Young Settlement is part of a CCAA plan process. Claims, including contingent claims, are regularly compromised and settled within CCAA proceedings. This includes outstanding litigation claims against the debtor and

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third parties. Such compromises fully and finally dispose of such claims, and it follows that there are no continuing procedural or other rights in such proceedings. Simply put, there are no "opt-outs" in the CCAA.

37 It is well established that class proceedings can be settled in a CCAA proceeding. See *Robertson v. ProQuest Information & Learning Co.*, 2011 ONSC 1647 (Ont. S.C.J. [Commercial List]) [*Robertson*].

38 As noted by Pepall J. (as she then was) in *Robertson*, para. 8:

> When dealing with the consensual resolution of a CCAA claim filed in a claims process that arises out of ongoing litigation, typically no court approval is required. In contrast, class proceedings settlements must be approved by the court. The notice and process for dissemination of the settlement agreement must also be approved by the court.

39 In this case, the notice and process for dissemination have been approved.

40 The Objectors take the position that approval of the Ernst & Young Settlement would render their opt-out rights illusory; the inherent flaw with this argument is that it is not possible to ignore the CCAA proceedings.

41 In this case, claims arising out of the class proceedings are claims in the CCAA process. CCAA claims can be, by definition, subject to compromise. The Claims Procedure Order establishes that claims as against Ernst & Young fall within the CCAA proceedings. Thus, these claims can also be the subject of settlement and, if settled, the claims of all creditors in the class can also be settled.

42 In my view, these proceedings are the appropriate time and place to consider approval of the Ernst & Young Settlement. This court has the jurisdiction in respect of both the CCAA and the CPA.

Should the Court Exercise Its Discretion to Approve the Settlement

43 Having established the jurisdictional basis to consider the motion, the central inquiry is whether the court should exercise its discretion to approve the Ernst & Young Settlement.

CCAA Interpretation

44 The CCAA is a "flexible statute", and the court has "jurisdiction to approve major transactions, including settlement agreements, during the stay period defined in the Initial Order". The CCAA affords courts broad jurisdiction to make orders and "fill in the gaps in legislation so as to give effect to the objects of the CCAA." [*Nortel Networks Corp., Re*, 2010 ONSC 1708 (Ont. S.C.J. [Commercial List]), paras. 66-70 ("*Re Nortel*")); *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 5 C.B.R. (4th) 299, 72 O.T.C. 99 (Ont. Gen. Div. [Commercial List]), para. 43]

45 Further, as the Supreme Court of Canada explained in *Ted Leroy Trucking Ltd., Re*, 2010 SCC 60 (S.C.C.), para. 58:

> CCAA decisions are often based on discretionary grants of jurisdiction. The incremental exercise of judicial discretion in commercial courts under conditions one practitioner aptly described as "the hothouse of real time litigation" has been the primary method by which the CCAA has been adapted and has evolved to meet contemporary business and social needs (internal citations omitted). ...When large companies encounter difficulty, reorganizations become increasingly complex. CCAA courts have been called upon to innovate accordingly in exercising their jurisdiction beyond merely staying proceedings against the Debtor to allow breathing room for reorganization. They have been asked to sanction measures for which there is no explicit authority in the CCAA.

46 It is also established that third-party releases are not an uncommon feature of complex restructurings under the CCAA [*ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.*, 2008 ONCA 587 (Ont. C.A.) ("*ATB Financial*"); *Nortel Networks Corp., Re, supra*; *Robertson, supra*; *Muscletech Research & Development Inc., Re* (2007), 30 C.B.R. (5th) 59, 156 A.C.W.S. (3d) 22 (Ont. S.C.J. [Commercial List]) ("*Muscle Tech*"); *Grace Canada Inc., Re* (2008), 50

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C.B.R. (5th) 25 (Ont. S.C.J. [Commercial List]); *Allen-Vanguard Corp., Re*, 2011 ONSC 5017 (Ont. S.C.J. [Commercial List])].

47 The Court of Appeal for Ontario has specifically confirmed that a third-party release is justified where the release forms part of a comprehensive compromise. As Blair J. A. stated in *ATB Financial, supra*:

> 69. In keeping with this scheme and purpose, I do not suggest that any and all releases between creditors of the debtor company seeking to restructure and third parties may be made the subject of a compromise or arrangement between the debtor and its creditors. Nor do I think the fact that the releases may be "necessary" in the sense that the third parties or the debtor may refuse to proceed without them, of itself, advances the argument in favour of finding jurisdiction (although it may well be relevant in terms of the fairness and reasonableness analysis).
>
> 70. The release of the claim in question must be justified as part of the compromise or arrangement between the debtor and its creditors. In short, there must be a reasonable connection between the third party claim being compromised in the plan and the restructuring achieved by the plan to warrant inclusion of the third party release in the plan ...
>
> 71. In the course of his reasons, the application judge made the following findings, all of which are amply supported on the record:
>
> > a) The parties to be released are necessary and essential to the restructuring of the debtor;
> >
> > b) The claims to be released are rationally related to the purpose of the Plan and necessary for it;
> >
> > c) The Plan cannot succeed without the releases;
> >
> > d) The parties who are to have claims against them released are contributing in a tangible and realistic way to the Plan; and
> >
> > e) The Plan will benefit not only the debtor companies but creditor Noteholders generally.
>
> 72. Here, then — as was the case in T&N — there is a close connection between the claims being released and the restructuring proposal. The tort claims arise out of the sale and distribution of the ABCP Notes and their collapse in value, just as do the contractual claims of the creditors against the debtor companies. The purpose of the restructuring is to stabilize and shore up the value of those notes in the long run. The third parties being released are making separate contributions to enable those results to materialize. Those contributions are identified earlier, at para. 31 of these reasons. The application judge found that the claims being released are not independent of or unrelated to the claims that the Noteholders have against the debtor companies; they are closely connected to the value of the ABCP Notes and are required for the Plan to succeed ...
>
> 73. I am satisfied that the wording of the CCAA — construed in light of the purpose, objects and scheme of the Act and in accordance with the modern principles of statutory interpretation — supports the court's jurisdiction and authority to sanction the Plan proposed here, including the contested third-party releases contained in it.
>
> . . .
>
> 78. ... I believe the open-ended CCAA permits third-party releases that are reasonably related to the restructuring at issue because they are encompassed in the comprehensive terms "compromise" and "arrangement" and because of the double-voting majority and court sanctioning statutory mechanism that makes them binding on unwilling creditors.
>
> . . .

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> 113. At para. 71 above I recited a number of factual findings the application judge made in concluding that approval of the Plan was within his jurisdiction under the CCAA and that it was fair and reasonable. For convenience, I reiterate them here — with two additional findings — because they provide an important foundation for his analysis concerning the fairness and reasonableness of the Plan. The application judge found that:
>
> a) The parties to be released are necessary and essential to the restructuring of the debtor;
>
> b) The claims to be released are rationally related to the purpose of the Plan and necessary for it;
>
> c) The Plan cannot succeed without the releases;
>
> d) The parties who are to have claims against them released are contributing in a tangible and realistic way to the Plan;
>
> e) The Plan will benefit not only the debtor companies but creditor Noteholders generally;
>
> f) The voting creditors who have approved the Plan did so with knowledge of the nature and effect of the releases; and that,
>
> g) The releases are fair and reasonable and not overly broad or offensive to public policy.

48 Furthermore, in *ATB Financial, supra*, para. 111, the Court of Appeal confirmed that parties are entitled to settle allegations of fraud and to include releases of such claims as part of the settlement. It was noted that "there is no legal impediment to granting the release of an antecedent claim in fraud, provided the claim is in the contemplation of the parties to the release at the time it is given".

Relevant CCAA Factors

49 In assessing a settlement within the CCAA context, the court looks at the following three factors, as articulated in *Robertson, supra*:

> (a) whether the settlement is fair and reasonable;
>
> (b) whether it provides substantial benefits to other stakeholders; and
>
> (c) whether it is consistent with the purpose and spirit of the CCAA.

50 Where a settlement also provides for a release, such as here, courts assess whether there is "a reasonable connection between the third party claim being compromised in the plan and the restructuring achieved by the plan to warrant inclusion of the third party release in the plan". Applying this "nexus test" requires consideration of the following factors: [*ATB Financial, supra*, para. 70]

> (a) Are the claims to be released rationally related to the purpose of the plan?
>
> (b) Are the claims to be released necessary for the plan of arrangement?
>
> (c) Are the parties who have claims released against them contributing in a tangible and realistic way? and
>
> (d) Will the plan benefit the debtor and the creditors generally?

Counsel Submissions

51 The Objectors argue that the proposed Ernst & Young Release is not integral or necessary to the success of Sino-Forest's restructuring plan, and, therefore, the standards for granting thirdparty releases in the CCAA are not satisfied.

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No one has asserted that the parties require the Ernst & Young Settlement or Ernst & Young Release to allow the Plan to go forward; in fact, the Plan has been implemented prior to consideration of this issue. Further, the Objectors contend that the $117 million settlement payment is not essential, or even related, to the restructuring, and that it is concerning, and telling, that varying the end of the Ernst & Young Settlement and Ernst & Young Release to accommodate opt-outs would extinguish the settlement.

52 The Objectors also argue that the Ernst & Young Settlement should not be approved because it would vitiate opt-out rights of class members, as conferred as follows in section 9 of the CPA: "Any member of a class involved in a class proceeding may opt-out of the proceeding in the manner and within the time specified in the certification order." This right is a fundamental element of procedural fairness in the Ontario class action regime [*Fischer v. IG Investment Management Ltd.*, 2012 ONCA 47 (Ont. C.A.), para. 69], and is not a mere technicality or illusory. It has been described as absolute [*Durling v. Sunrise Propane Energy Group Inc.*, 2011 ONSC 266 (Ont. S.C.J.)]. The opt-out period allows persons to pursue their self-interest and to preserve their rights to pursue individual actions [*Mangan v. Inco Ltd.* (1998), 16 C.P.C. (4th) 165, 38 O.R. (3d) 703 (Ont. Gen. Div.)].

53 Based on the foregoing, the Objectors submit that a proposed class action settlement with Ernst & Young should be approved solely under the CPA, as the Pöyry Settlement was, and not through misuse of a third-party release procedure under the CCAA. Further, since the minutes of settlement make it clear that Ernst & Young retains discretion not to accept or recognize normal opt-outs if the CPA procedures are invoked, the Ernst & Young Settlement should not be approved in this respect either.

54 Multiple parties made submissions favouring the Ernst & Young Settlement (with the accompanying Ernst & Young Release), arguing that it is fair and reasonable in the circumstances, benefits the CCAA stakeholders (as evidenced by the broad-based support for the Plan and this motion) and rationally connected to the Plan.

55 Ontario Plaintiffs' counsel submits that the form of the bar order is fair and properly balances the competing interests of class members, Ernst & Young and the non-settling defendants as:

(a) class members are not releasing their claims to a greater extent than necessary;

(b) Ernst & Young is ensured that its obligations in connection to the Settlement will conclude its liability in the class proceedings;

(c) the non-settling defendants will not have to pay more following a judgment than they would be required to pay if Ernst & Young remained as a defendant in the action; and

(d) the non-settling defendants are granted broad rights of discovery and an appropriate credit in the ongoing litigation, if it is ultimately determined by the court that there is a right of contribution and indemnity between the co-defendants.

56 SFC argues that Ernst & Young's support has simplified and accelerated the Plan process, including reducing the expense and management time otherwise to be incurred in litigating claims, and was a catalyst to encouraging many parties, including the Underwriters and BDO, to withdraw their objections to the Plan. Further, the result is precisely the type of compromise that the CCAA is designed to promote; namely, Ernst & Young has provided a tangible and significant contribution to the Plan (notwithstanding any pitfalls in the litigation claims against Ernst & Young) that has enabled SFC to emerge as Newco/NewcoII in a timely way and with potential viability.

57 Ernst & Young's counsel submits that the Ernst & Young Settlement, as a whole, including the Ernst & Young Release, must be approved or rejected; the court cannot modify the terms of a proposed settlement. Further, in deciding whether to reject a settlement, the court should consider whether doing so would put the settlement in "jeopardy of being unravelled". In this case, counsel submits there is no obligation on the parties to resume discussions and it could be that the parties have reached their limits in negotiations and will backtrack from their positions or abandon the effort.

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Analysis and Conclusions

58 The Ernst & Young Release forms part of the Ernst & Young Settlement. In considering whether the Ernst & Young Settlement is fair and reasonable and ought to be approved, it is necessary to consider whether the Ernst & Young Release can be justified as part of the Ernst & Young Settlement. See *ATB Financial*, *supra*, para. 70, as quoted above.

59 In considering the appropriateness of including the Ernst & Young Release, I have taken into account the following.

60 Firstly, although the Plan has been sanctioned and implemented, a significant aspect of the Plan is a distribution to SFC's creditors. The significant and, in fact, only monetary contribution that can be directly identified, at this time, is the $117 million from the Ernst & Young Settlement. Simply put, until such time as the Ernst & Young Settlement has been concluded and the settlement proceeds paid, there can be no distribution of the settlement proceeds to parties entitled to receive them. It seems to me that in order to effect any distribution, the Ernst & Young Release has to be approved as part of the Ernst & Young Settlement.

61 Secondly, it is apparent that the claims to be released against Ernst & Young are rationally related to the purpose of the Plan and necessary for it. SFC put forward the Plan. As I outlined in the Equity Claims Decision, the claims of Ernst & Young as against SFC are intertwined to the extent that they cannot be separated. Similarly, the claims of the Objectors as against Ernst & Young are, in my view, intertwined and related to the claims against SFC and to the purpose of the Plan.

62 Thirdly, although the Plan can, on its face, succeed, as evidenced by its implementation, the reality is that without the approval of the Ernst & Young Settlement, the objectives of the Plan remain unfulfilled due to the practical inability to distribute the settlement proceeds. Further, in the event that the Ernst & Young Release is not approved and the litigation continues, it becomes circular in nature as the position of Ernst & Young, as detailed in the Equity Claims Decision, involves Ernst & Young bringing an equity claim for contribution and indemnity as against SFC.

63 Fourthly, it is clear that Ernst & Young is contributing in a tangible way to the Plan, by its significant contribution of $117 million.

64 Fifthly, the Plan benefits the claimants in the form of a tangible distribution. Blair J.A., at paragraph 113 of *ATB Financial*, *supra*, referenced two further facts as found by the application judge in that case; namely, the voting creditors who approved the Plan did so with the knowledge of the nature and effect of the releases. That situation is also present in this case.

65 Finally, the application judge in *ATB Financial*, *supra*, held that the releases were fair and reasonable and not overly broad or offensive to public policy. In this case, having considered the alternatives of lengthy and uncertain litigation, and the full knowledge of the Canadian plaintiffs, I conclude that the Ernst & Young Release is fair and reasonable and not overly broad or offensive to public policy.

66 In my view, the Ernst & Young Settlement is fair and reasonable, provides substantial benefits to relevant stakeholders, and is consistent with the purpose and spirit of the CCAA. In addition, in my view, the factors associated with the *ATB Financial* nexus test favour approving the Ernst & Young Release.

67 In *Nortel Networks Corp., Re*, *supra*, para. 81, I noted that the releases benefited creditors generally because they "reduced the risk of litigation, protected Nortel against potential contribution claims and indemnity claims and reduced the risk of delay caused by potentially complex litigation and associated depletion of assets to fund potentially significant litigation costs". In this case, there is a connection between the release of claims against Ernst & Young and a distribution to creditors. The plaintiffs in the litigation are shareholders and Noteholders of SFC. These plaintiffs have claims to assert against SFC that are being directly satisfied, in part, with the payment of $117 million by Ernst & Young.

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68 In my view, it is clear that the claims Ernst & Young asserted against SFC, and SFC's subsidiaries, had to be addressed as part of the restructuring. The interrelationship between the various entities is further demonstrated by Ernst & Young's submission that the release of claims by Ernst & Young has allowed SFC and the SFC subsidiaries to contribute their assets to the restructuring, unencumbered by claims totalling billions of dollars. As SFC is a holding company with no material assets of its own, the unencumbered participation of the SFC subsidiaries is crucial to the restructuring.

69 At the outset and during the CCAA proceedings, the Applicant and Monitor specifically and consistently identified timing and delay as critical elements that would impact on maximization of the value and preservation of SFC's assets.

70 Counsel submits that the claims against Ernst & Young and the indemnity claims asserted by Ernst & Young would, absent the Ernst & Young Settlement, have to be finally determined before the CCAA claims could be quantified. As such, these steps had the potential to significantly delay the CCAA proceedings. Where the claims being released may take years to resolve, are risky, expensive or otherwise uncertain of success, the benefit that accrues to creditors in having them settled must be considered. See *Nortel Networks Corp., Re*, *supra*, paras. 73 and 81; and *Muscletech*, *supra*, paras. 19-21.

71 Implicit in my findings is rejection of the Objectors' arguments questioning the validity of the Ernst & Young Settlement and Ernst & Young Release. The relevant consideration is whether a proposed settlement and third-party release sufficiently benefits all stakeholders to justify court approval. I reject the position that the $117 million settlement payment is not essential, or even related, to the restructuring; it represents, at this point in time, the only real monetary consideration available to stakeholders. The potential to vary the Ernst & Young Settlement and Ernst & Young Release to accommodate opt-outs is futile, as the court is being asked to approve the Ernst & Young Settlement and Ernst & Young Release as proposed.

72 I do not accept that the class action settlement should be approved solely under the CPA. The reality facing the parties is that SFC is insolvent; it is under CCAA protection, and stakeholder claims are to be considered in the context of the CCAA regime. The Objectors' claim against Ernst & Young cannot be considered in isolation from the CCAA proceedings. The claims against Ernst & Young are interrelated with claims as against SFC, as is made clear in the Equity Claims Decision and Claims Procedure Order.

73 Even if one assumes that the opt-out argument of the Objectors can be sustained, and optout rights fully provided, to what does that lead? The Objectors are left with a claim against Ernst & Young, which it then has to put forward in the CCAA proceedings. Without taking into account any argument that the claim against Ernst & Young may be affected by the claims bar date, the claim is still capable of being addressed under the Claims Procedure Order. In this way, it is again subject to the CCAA fairness and reasonable test as set out in *ATB Financial*, *supra*.

74 Moreover, CCAA proceedings take into account a class of creditors or stakeholders who possess the same legal interests. In this respect, the Objectors have the same legal interests as the Ontario Plaintiffs. Ultimately, this requires consideration of the totality of the class. In this case, it is clear that the parties supporting the Ernst & Young Settlement are vastly superior to the Objectors, both in number and dollar value.

75 Although the right to opt-out of a class action is a fundamental element of procedural fairness in the Ontario class action regime, this argument cannot be taken in isolation. It must be considered in the context of the CCAA.

76 The Objectors are, in fact, part of the group that will benefit from the Ernst & Young Settlement as they specifically seek to reserve their rights to "opt-in" and share in the spoils.

77 It is also clear that the jurisprudence does not permit a dissenting stakeholder to opt-out of a restructuring. [*Sammi Atlas Inc., Re* (1998), 3 C.B.R. (4th) 171 (Ont. Gen. Div. [Commercial List])).] If that were possible, no creditor would take part in any CCAA compromise where they were to receive less than the debt owed to them. There is no right to

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opt-out of any CCAA process, and the statute contemplates that a minority of creditors are bound by the plan which a majority have approved and the court has determined to be fair and reasonable.

78 SFC is insolvent and all stakeholders, including the Objectors, will receive less than what they are owed. By virtue of deciding, on their own volition, not to participate in the CCAA process, the Objectors relinquished their right to file a claim and take steps, in a timely way, to assert their rights to vote in the CCAA proceeding.

79 Further, even if the Objectors had filed a claim and voted, their minimal 1.6% stake in SFC's outstanding shares when the Muddy Waters report was released makes it highly unlikely that they could have altered the outcome.

80 Finally, although the Objectors demand a right to conditionally opt-out of a settlement, that right does not exist under the CPA or CCAA. By virtue of the certification order, class members had the ability to opt-out of the class action. The Objectors did not opt-out in the true sense; they purported to create a conditional opt-out. Under the CPA, the right to opt-out is "in the manner and within the time specified in the certification order". There is no provision for a conditional opt-out in the CPA, and Ontario's single opt-out regime causes "no prejudice...to putative class members". [CPA, section 9; *Osmun v. Cadbury Adams Canada Inc.* (2009), 85 C.P.C. (6th) 148 (Ont. S.C.J.), paras. 43-46; and *Eidoo v. Infineon Technologies AG*, 2012 ONSC 7299 (Ont. S.C.J.).]

Miscellaneous

81 For greater certainty, it is my understanding that the issues raised by Mr. O'Reilly have been clarified such that the effect of this endorsement is that the Junior Objectors will be included with the same status as the Ontario Plaintiffs.

Disposition

82 In the result, for the foregoing reasons, the motion is granted. A declaration shall issue to the effect that the Ernst & Young Settlement is fair and reasonable in all the circumstances. The Ernst & Young Settlement, together with the Ernst & Young Release, is approved and an order shall issue substantially in the form requested. The motion of the Objectors is dismissed.

Motion granted.

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TAB 6

1993 CarswellOnt 801
Supreme Court of Canada

Queen v. Cognos Inc.

1993 CarswellOnt 801, 1993 CarswellOnt 972, [1993] 1 S.C.R. 87, [1993] S.C.J. No. 3, 147 N.R. 169, 14 C.C.L.T. (2d) 113, 37 A.C.W.S. (3d) 1304, 45 C.C.E.L. 153, 60 O.A.C. 1, 93 C.L.L.C. 14,019, 99 D.L.R. (4th) 626, J.E. 93-270, D.T.E. 93T-198, EYB 1993-67486

DOUGLAS J. QUEEN v. COGNOS INCORPORATED

La Forest, L'Heureux-Dubé, Sopinka, Gonthier, McLachlin, Stevenson * and Iacobucci JJ.

Heard: January 29, 1992
Judgment: January 21, 1993
Docket: Doc. n° 22004

Counsel: *Peter J. Bishop* and *Tom Brooker* , for appellant
Charles T. Hackland and *Mark Josselyn* , for respondent

Subject: Torts; Employment; Civil Practice and Procedure; Contracts; Corporate and Commercial

Appeal from judgment reported at (1990), 30 C.C.E.L. 1, 38 O.A.C. 180, 69 D.L.R. (4th) 288, 74 O.R. (2d) 176, 90 C.L.L.C. 14,024 (C.A.) , setting aside judgment reported at (1987), 18 C.C.E.L. 146, 63 O.R. (2d) 389 (H.C.) , awarding damages in claim for negligent misrepresentation.

***La Forest J.* (*L'Heureux-Dubé* and *Gonthier JJ.* concurring):**

1 Subject to what I have had to say in *BG Checo International Ltd. v. British Columbia Hydro & Power Authority* , S.C.C., Nos. 21939 and 21955, issued concurrently [reported 75 B.C.L.R. (2d) 145], I agree with Justices Iacobucci and McLachlin, and would dispose of the appeal in the manner proposed by them. Though Iacobucci J. repeats the essence of his analysis in *Checo* , the present case is not one of concurrency at all. It is sufficient for me to say that the tort here was independent of the contract and the liability was not limited by an exclusion clause in the contract.

***Iacobucci J.* (*Sopinka J.* concurring):**

2 This appeal involves the application of the tort of negligent misrepresentation to a pre-employment representation made by an employer to a prospective employee in the course of a hiring interview. Specifically, this court is being asked to determine in what circumstances a representation made during a hiring interview becomes, in law, a "negligent misrepresentation". A subsidiary question deals with the effect of a subsequent employment agreement signed by the plaintiff, and its provisions allowing termination "without cause" and reassignment, on a claim for damages for negligent misrepresentation.

I. Facts

3 The trial judge conducted an extensive and thorough review of the facts in the course of his reasons for judgment. None of his findings of fact has been challenged in a direct manner by the respondent or altered by the Court of Appeal. As the facts are particularly important in the case at bar, I will review in some detail the trial judge's most relevant findings.

4 The respondent, Cognos Incorporated (previously named Quasar Corporation and hereinafter referred to as "Cognos" or "respondent"), is an Ottawa-based company which carries on the business of designing, developing and

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marketing computer programmes and software. In December of 1982, the respondent's president (Mr. Mike Potter) instructed Mr. Sean Johnston, the recently appointed manager of product development for a product line of accounting software known as "Multiview", that Cognos intended to develop Multiview to an equal standing with its main product line called "Power House". Mr. Johnston had also received instructions from the vice-president of research and development of Cognos (Mr. Bob Minns), at the time of accepting the position of manager of product development, that the respondent wished to see Multiview expand beyond the general ledger module (the software involved consists of various "modules") then developed and in circulation, and the accounts payable module then under development. In particular, he was told that the respondent wished to see the development of three additional modules, namely, accounts receivable, cash flow, and fixed assets. Mr. Johnston was instructed by Cognos's senior management to take charge and to do whatever was necessary to make Multiview a marketable and profitable product.

5 A meeting was held on December 21, 1982, during which Mr. Johnston and several senior executives of Cognos reviewed plans for the development of the Multiview line of products according to the mandate that had just been given. Criticisms were voiced by Mr. Johnston about the development of Multiview currently under way. He filed a project schedule covering a period of time up to 1985 and contemplating the development of modules such as accounts payable, accounts receivable, and cash flow.

6 Mr. Johnston indicated that there was a need on the research and development team of Multiview for an accountant to assist in the writing and maintenance of the software. Mr. Johnston proceeded, with the full knowledge of the respondent's senior management, to advertise for (and later hire) an accountant to help with the development of Multiview. An advertisement was placed in *The Globe and Mail* in mid-January, 1983, and many responses were received. In February of that year, a short list of six chartered accountants were interviewed by Mr. Johnston and two other executives of Cognos. The appellant, Douglas J. Queen, was one of the persons interviewed.

7 At the time of his interview, the appellant had been qualified as a chartered accountant for some eight and a half years. Since May of 1975, he had been living in Calgary with his wife and children and had occupied positions with three different employers, whereby he gained experience in working with computer accounting systems. For the three and a half years prior to the interview, the appellant had been the regional controller for a Calgary-based corporation named Genstar Development Corporation, occupying a relatively well paying and secure managerial position. In the fall of 1982, the appellant was actively seeking employment outside Calgary and was interested in the high-tech industry in the Ottawa area. In the words of the trial judge, the appellant wanted more challenging opportunities than were available for him in Calgary; he wanted a senior financial position that would make use of his expertise in management information computer systems.

8 On February 14, 1983, the appellant was interviewed for approximately an hour and a half. During this interview, Mr. Johnston made a number of representations (as he had to the other five candidates) about the Multiview project and about the successful candidate's role in its development. These representations are fully canvassed at pp. 396-98 of the reported reasons of the trial judge: (1987), 63 O.R. (2d) 389 .

9 In sum, Mr. Johnston told the appellant that Multiview was a major project which would be developed over a period of two years (the "primary development period") with enhancements and maintenance thereafter, and that the position being interviewed for would be needed throughout this period. It was made clear that Cognos was committed to the development of additional modules of Multiview beyond general ledger (then developed), accounts payable (development under way), and accounts receivable (planned, but not yet under development). Those additional modules were cash flow, fixed assets, inventory, and order entry. Moreover, it was represented that the staff required to develop the Multiview modules would double, from 16 to 32, by August, 1983 (the appellant's evidence), or by the end of the two year primary development period (Mr. Johnston's evidence). Throughout the interview, it was understood that the successful candidate would play an important role as a chartered accountant in the Multiview project, advising on accounting standards throughout the life of the project. In addition, the trial judge found, based on his assessment of all the evidence, that it was implicitly represented that there was a reasonable plan in existence for the additional modules and that Cognos had made a financial commitment for such development in the way of budgetary provisions.

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10 At the time of this interview, Mr. Johnston's knowledge as to the respondent's commitment to the development of Multiview was based on conversations and meetings with senior executives of Cognos. He was aware, however, that the funding needed for the full development of Multiview in accordance with his mandate had not yet been approved by the respondent's corporate management team. While this body had met in early February to discuss and formulate strategies and plans for the development of Multiview, it had not yet given any financial commitment commensurate with the mandate given to Mr. Johnston. Mr. Johnston was also aware that this body had the ultimate responsibility of deciding whether to allocate corporate funds for the research and development of Multiview. At no point during the interview was the appellant made aware of the fact that there was no guaranteed funding for the Multiview project as described to him, or that the position being applied for was subject, in any respect, to budgetary approval.

11 The appellant was offered the job of manager, financial standards, by telephone early in the month of March, 1983. He accepted immediately and Mr. Johnston mailed to him a written contract of employment. It is undisputed that, prior to signing, the appellant read and understood the employment agreement. He knew that its purpose was to define the rights and obligations of the parties. One clause in the contract (clause 14) permitted the respondent to terminate at any time the appellant's employment "without cause" upon one month's notice, or payment of one month's salary in lieu of notice. Another clause (clause 13) enabled the respondent to reassign the appellant to another position within Cognos without reduction in salary and upon one month's notice. Much importance was given to these provisions by the Court of Appeal as well as by the respondent in argument before this court.

12 For convenience, I shall reproduce clauses 13 and 14 of the employment agreement:

Transfer

> 13. Quasar Systems reserves the right to reassign you to another position with the Company without reduction of your salary or benefits and upon one month's notice to you. Should such reassignment require your permanent relocation to another city, the Company will reimburse you for your expenses in accordance with the then current relocation policy.

Termination Notice — One Month

> 14. This Agreement may be terminated at any time and without cause by Quasar Systems Ltd. or by you. In the event of termination, Quasar Systems Ltd. will give you one month's notice of termination plus any additional notice that may be required by any applicable legislation. Similarly, you shall give Quasar Systems Ltd. one month's notice if you voluntarily terminate this Agreement. Quasar Systems Ltd. may pay you one month's salary in lieu of the aforesaid notice in which event this Agreement and your employment will be terminated on the date such payment in lieu of notice is made.

13 The trial judge specifically accepted the appellant's evidence that he signed the contract of employment based on the representations made to him during the interview, and that were it not for those representations he would not have signed it. In order to accept employment with Cognos, the appellant was required to give up a relatively well paying and secure, albeit not as challenging, position in Calgary and to move himself and his family more than half-way across the country.

14 The appellant commenced employment with Cognos on April 11, 1983. Two weeks later, on April 25, 1983, the corporate management team of the respondent considered for the very first time the project cost estimates for the Multiview project. This body rejected Mr. Johnston's funding proposal which was in excess of $1,000,000. It decided to commit research and development funds to the Power House project in priority to Multiview. This decision was based on a number of market considerations, including the continuing low sales of the then developed Multiview module (general ledger) and the continuing high sales of the various Power House modules. The corporate management team allotted a budget of only $200,000 to Multiview, thus making the development of additional modules beyond accounts receivable quite unrealistic. Further meetings of the management team took place in the following months at which time additional funding curtailment of the Multiview project occurred. On September 9, 1983, barely five months after his arrival in

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Ottawa, the appellant and others were advised that there would be a reassignment of personnel involved with Multiview owing to diminished research and development funding. The appellant was informed that, unless a position was available for him in the finance and administration department of the respondent, he would most likely be laid off.

15 On October 28, 1983, the appellant was given his first written notice of termination of employment effective March 21, 1984. The appellant negotiated an amendment to his employment agreement in order to eliminate his obligation to repay $7,500 of moving expenses, otherwise repayable in the event that his position was terminated within the first year of employment. This notice was rescinded in November, 1983, and the appellant was assigned to quality control of one of the aspects of the Power House project. On May 1, 1984, after having been informed earlier in March that he would no longer be needed with quality control, the appellant secured the position of manager of finance in the finance department of the respondent. He performed various tasks while in this function. On July 31, 1984, he received his second written notice of termination effective October 25, 1984. He worked until that day and was paid until November 15, 1984. The trial judge found that the appellant was not dismissed as a result of an unsatisfactory assessment of his job performance.

16 On March 25, 1985, the appellant commenced an action against the respondent seeking damages for negligent and fraudulent misrepresentation. He apparently discontinued his claim for fraudulent misrepresentation at some point after filing the statement of claim, and proceeded only in negligence. From the beginning, the appellant's cause of action has been founded wholly and solely in tort. At no time did he argue breach of contract, breach of collateral warranty or any other contractual cause of action against the respondent. He did not dispute the fact that some of the terms of his employment contract ap peared to be inconsistent with the representations made by Mr. Johnston. However, it was his understanding from the interview that the Multiview project was a reality and that its existence was not contingent on the happening of some future event. He testified that were it not for the representations made during the interview as to the nature and existence of the employment opportunity, he would not have left his secure position in Calgary.

17 In a judgment rendered on December 31, 1987, White J. of the Ontario High Court of Justice upheld the appellant's claim and awarded him $67,224 in damages: (1987), 18 C.C.E.L. 146 , 63 O.R (2d) 389. On May 1, 1990, an appeal by the respondent to the Court of Appeal for Ontario was allowed; the trial judgment was set aside and replaced by a judgment dismissing the action with costs: (1990), 30 C.C.E.L. 1, 38 O.A.C. 180, 69 D.L.R. (4th) 288, 74 O.R. (2d) 176, 90 C.L.L.C. 14,024 . The appellant was granted leave to appeal to this court on January 17, 1991, [1991] 1 S.C.R. xii.

II. Judgments in the Courts Below

A. Ontario High Court of Justice (1987), 63 O.R. (2d) 389

18 The trial judge found, in all the circumstances, that there existed a "special relationship" between the respondent (via Mr. Johnston) and the appellant, within the meaning of *Hedley Byrne & Co. v. Heller & Partners Ltd.*, [1964] A.C. 465 (H.L.) , so as to give rise to a duty of care with respect to the representations made during the hiring interview. The fact that this case involved pre-contractual or pre-employment negotiations did not alter this conclusion. Based on his assessment of all the evidence adduced at trial, White J. also found that certain representations made to the appellant during the interview were inaccurate or misleading (i.e., they were misrepresentations), and that these misrepresentations were made in a negligent manner (i.e., they were *negligent* misrepresentations). Some of his comments in this respect warrant repeating (at pp. 415-16):

> I find that misrepresentations were made to the [appellant] by Sean Johnston in the hiring interview. The effect of these misrepresentations was that the [appellant] would have a position in the research and development of the product "Multiview"; that that position would be a significant one and would involve his expertise as an accountant; that he would perform the responsible role of seeing to proper accounting standards being implemented into the product; that beyond the three modules immediately in contemplation were a minimum of four other modules; and that the project of "Multiview", in connection with which [the appellant] would be hired would last a minimum of two years. I find further that Mr. Johnston implicitly represented that management had made a firm budgetary commit ment to the development of four other modules in addition to those then presently under development.

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> I find further, in all the circumstances, that Sean Johnston made those misrepresentations negligently. Based upon his expertise in the field of computer development, he was aware, according to his evidence, that until there is a feasibility study in which cost estimates have been submitted to and have been considered and approved by senior management, one could not say that the [respondent] had made a firm commitment to the project as Mr. Johnston envisaged it and as he described it to [the appellant] in the interview.

19 Other circumstances which the trial judge took into consideration in concluding that the misrepresentations were negligently made include the following: (1) Mr. Johnston knew, or ought to have known, that the truth of his representations depended on the approval by the corporate management team of the cost estimates he had prepared for the research and development of the Multiview project; (2) it is reasonable to infer that Mr. Johnston, at the time of the interview, contemplated that the budgetary needs for the Multiview project would be substantial and that approval was at best speculative; (3) Mr. Johnston must have been aware of the continued poor sales performance of the Multiview product line; (4) Mr. Johnston did not disclose to the appellant that senior management had not yet given the financial commitment required to make the plans for the Multiview project a probable reality; (5) Mr. Johnston's expertise in the computer development field should have made him aware that, notwithstanding his conversations with senior management and the meeting of December 21, 1982, there was still a considerable risk that senior management would not give budgetary approval to his plans; (6) Mr. Johnston knew that the appellant was relying on the information he was providing during the interview; (7) Mr. Johnston knew that the appellant had a secure, responsible, and well-paying employment as a chartered accountant in Calgary and that coming to Ottawa would involve moving himself and his family across the country; and (8) Mr. Johnston was aware that the appellant was relying on the position with Cognos to enhance his career significantly as an accountant.

20 The trial judge also found that, even if Mr. Johnston felt justified in making the representations that he did (based on his conversations with senior management and the meeting of December 21, 1982), and assuming that this deprived his misrepresentations of their negligent quality, then such misrepresentations, while not negligently made by Mr. Johnston, were negligently made by the senior management of the respondent "through Mr. Johnston as an innocent instrument of the [respondent] company" (p.418).

21 White J. further found that the appellant had relied upon the negligent misrepresentations, to his detriment, and that he had sus tained substantial damages (at p. 419):

> The misrepresentations induced [the appellant] to quit his job as controller of the Calgary Division of Genstar Development Corporation and to accept employment with the [respondent]. Those representations induced him to sign the contract of employment. But for those representations he would have remained working for the Genstar Development Corporation for some further period of time and would not have become an employee of the [respondent].

22 Finally, the trial judge addressed a number of arguments raised by the respondent in defence. First, he rejected the proposition that the representations were truthful and that Mr. Johnston was simply giving an opinion as to future events. In his view, the representations were untruthful: "What was untruthful in the representations was the implied assurance in those representations that Mr. Johnston had made a sufficient study of the relevant facts including the decision of senior management to make a financial commitment to the development of 'Multiview' beyond the accounts receivable module, to be able to make the unqualified representations that he made" (pp. 417-18). All Mr. Johnston had to say, in the trial judge's opinion, was that the feasibility study of the project had not yet been completed. Second, senior management of the respondent made no attempt to disclaim expressly any representations made to the appellant during the interview. Third, the trial judge rejected the defence put forward that the appellant, by his conduct subsequent to learning the situation of Multiview, had affirmed his contract of employment. In this respect, White J. distinguished the decision relied on by the respondent (*Burrows v. Burke* (1984), 49 O.R. (2d) 76 (C.A.)), and held that the appellant's conduct was not one of affirming the contract of employment but of a person in a difficult situation attempting to "minimize his damages" (p. 420). In any event, his conduct "did not amount to an explicit waiver of his right to claim

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damages in tort arising out of negligent misrepresentations made to him inducing the contract" (p. 421). In his view, whether the contract is affirmed or not, the cause of action in tort is preserved as it is external to the contract. And fourth, the trial judge rejected the respondent's defence of business necessity on the basis that there was no evidence of any such necessity which would exonerate the respondent from the negligent misrepresentations in issue.

23 Thus, White J. allowed the appellant's claim for negligent misrepresentation. He assessed the damages payable to the appellant at $67,224. This amount represented what was necessary, according to White J., "to put the [appellant] in the same position as he would have been if the negligent misrepresentation had not been made" (p.414). It consists of $50,000 for loss of income, $252 for costs of obtaining a new employment, $11,972 for the loss on the purchase and sale of his home in the Ottawa area, and $5,000 in general damages for emotional stress.

B. Ontario Court of Appeal (1990), 74 O.R. (2d) 176

24 Finlayson J.A. (Griffiths and Arbour JJ.A. concurring) held that the trial judge made two errors in allowing the appellant's claim to succeed. Finlayson J.A. accepted that there was a "special relationship" between the appellant and the respondent so as to give rise to a duty of care of the sort described in *Hedley Byrne* , supra, and subsequent cases. However, he was of the view that, in the circumstances of the present case, White J. had erred in the manner in which he dealt with the issues of contractual disclaimer and of negligence.

25 With respect to disclaimer, Finlayson J.A. felt the trial judge had erred in requiring an express disavowal of any representations that may have been made during the pre-contractual negotiations in order for a disclaimer argument to succeed, as it had in *Hedley Byrne* , supra, and in *Carman Construction Ltd. v. Canadian Pacific Railway*, [1982] 1 S.C.R. 958 . In Finlayson J.A.'s opinion, something less than an express disclaimer could suffice (at p. 183): "it is a sufficient disclaimer if the contract contains terms which contradict or are inconsistent with the representations relied upon." He noted that the contract of employment, which the appellant read and understood, contained provisions relating to the possibility of reassignment and, more importantly, to the termination of employment on one month's notice. He found that such provisions were sufficient to constitute a valid disclaimer (at pp. 183 and 185):

> In the case on appeal, the [appellant] stated that he would not have given up his secure position in Calgary for a move to Ottawa that was without permanence, and yet he signed a contract which provided him with no assurances respecting his place of employment or its tenure. To rely on *Hedley Byrne* , the negligent misrepresentation must have amounted to a warranty of job security and yet the contract of employment was surely a disclaimer of just that. No representations as to job security, whether based on performance or on job availability, could have survived the one-month termination notice "without cause" contained in the contract.
>
> .....
>
> The pre-employment discussions in this case merged in the contract of employment. There is no separate tort, even accepting the trial judge's findings of innocent misrepresentation, because the terms of the contract amounted to a disclaimer within the meaning of *Hedley Byrne* . The references to the Multiview project did not amount to warranties or representations that were independent of the contract of employment and they cannot survive the written agreement.

According to Finlayson J.A., this disclaimer was fatal to the appellant's claim as it had the effect of negating any assumption of duty of care on the part of the respondent; a conclusion similar to the one reached in *Hedley Byrne* and *Carman Construction* , supra.

26 In any event, Finlayson J.A. was of the view that the trial judge had erred in his finding of *negligent* misrepresentation because he imposed a "higher duty of care" on the respondent than was required in the circumstances. According to Finlayson J.A., the duty in the case at bar is no more than a duty to take care that the representations made were "responsible and accurate to the knowledge of Johnston and of his principal, Cognos" (p. 186). He observed that the same representations were made to all the six candidates, that the purpose of the interview was to make the position

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sound attractive enough that the successful candidate would accept it, and that Mr. Johnston believed in the veracity of what he was saying during the interview. Moreover, he noted that the trial judge criticized more what was not said by Mr. Johnston, than what was actually said by him. In his view, any duty of care had been fully discharged in the circumstances of this case — there had been no *negligent* misrepresentation (at pp. 187-88):

> Johnston was hired to oversee the Multiview project. Counsel for [the appellant] conceded that Johnston was as surprised as anyone at the corporate decision not to concentrate on it. Johnston believed in what he said to the job applicants about Multiview. The trial judge found that he had a duty to go further and to point out the details of the internal decision-making process at Cognos and stress that that process had not been completed. In other words, his own *bona fide* belief as a knowledgeable executive that the program was going forward was not sufficient. He had to divulge to all of the applicants that he interviewed the precise status of the corporate commitment to the development of the new product so that they could make their own assessment of the viability of the project.
>
> In my opinion, this casts the duty too high. It suggests that at least a quasi-fiduciary relationship existed between corporation and job applicant, giving rise to a duty to make full disclosure. Such a duty can exist in a given "special relationship" required by *Hedley Byrne* ...but it does not exist in this one. The trial judge was in error in extending to this situation the narrow class of contract cases where *uberrima fides* is the standard.
>
> .....
>
> In my opinion, while a "special relationship" existed between [the respondent] and the six applicants, any duty of care that arose from it was discharged. I say this without reference to the disclaimer in [the appellant's] contract. Johnston was not obliged to go father than he did in describing the job prospects. What he said was truthful, he believed in it, that was enough.

27 There was an appeal and cross-appeal as to damages. Finlayson J.A. held that if, contrary to his view, the appellant's action was successful, he would not have interfered with the assessment of damages made by the trial judge.

III. Issues

28 I would characterize the issues raised by this appeal as follows:

> (1) Disregarding for now the employment agreement signed by the appellant in March of 1983, did the respondent or its representative Mr. Johnston owe a duty of care to the appellant during the pre-employment interview of February 14, 1983, with respect to the representations made to the appellant about the respondent and the nature and existence of the employment opportunity being offered?
>
> (2) If so, again disregarding for now the contract between the parties, did the respondent or its representative Mr. Johnston breach this duty of care in all the circumstances of this case?
>
> (3) If so, should the answers given to questions 1 and 2, or the result that would normally follow from such conclusions (i.e. liability of the respondent for the damages caused to the appellant, fixed by the trial judge at $67,224, upheld by the Court of Appeal, and unchallenged before this court), be different in any way in view of the fact that the appellant signed an employment agreement after the negligent misrepresentations containing, inter alia, a termination "without cause" provision (clause 14) as well as a reassignment provision (clause 13)?

29 For reasons that follow, I am of the opinion that questions 1 and 2 should be answered in the affirmative and that question 3 should be answered in the negative. The appeal should therefore be allowed and the judgment of White J. in favour of the appellant and granting him damages in the amount of $67,224 should be restored.

IV. Analysis

30

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A. Introduction

31 This appeal involves an action in tort to recover damages caused by alleged negligent misrepresentations made in the course of a hiring interview by an employer (the respondent), through its representative, to a prospective employee (the appellant) with respect to the employer and the nature and existence of the employment opportunity. Though a relatively recent feature of the common law, the tort of negligent misrepresentation relied on by the appellant and first recognized by the House of Lords in *Hedley Byrne* , supra, is now an established principle of Canadian tort law. This court has confirmed on many occasions, sometimes tacitly, that an action in tort may lie, in appropriate circumstances, for damages caused by a misrepresentation made in a negligent manner: see *Welbridge Holdings Ltd. v. Winnipeg (City)*, [1971] S.C.R. 957 ; *J. Nunes Diamonds Ltd. v. Dominion Electric Protection Co.*, [1972] S.C.R. 769 ; *Rivtow Marine Ltd. v. Washington Iron Works*, [1974] S.C.R. 1189 ; *Hodgins v. Nepean Hydro-Electric Commission*, [1976] 2 S.C.R. 501 ; *The Pas (Town) v. Porky Packers Ltd.*, [1977] 1 S.C.R. 51 ; *Haig v. Bamford*, [1977] 1 S.C.R. 466 ; *Carman Construction* , supra; *V.K. Mason Construction Ltd. v. Bank of Nova Scotia*, [1985] 1 S.C.R. 271 ; and *Rainbow Industrial Caterers Ltd. v. Canadian National Railway Co.*, [1991] 3 S.C.R. 3 .

32 While the doctrine of *Hedley Byrne* , supra, is well established in Canada, the exact breadth of its applicability is, like any common law principle, subject to debate and to continuous development. At the time this appeal was heard, there have only been a handful of cases where the tort of negligent misrepresentation was used in a pre-employment context such as the one involved here: see *Steer v. Aerovox Inc.* (1984), 65 N.S.R. (2d) 91 (S.C.T.D.) ; *Wooldridge v. H.B. Nickerson & Sons Ltd.* (1980), 115 D.L.R. (3d) 97 (N.S.S.C.A.D.) ; *Williams v. Saanich School District No. 63* (1986), 11 C.C.E.L. 233 (B.C.S.C.) , affirmed on other grounds (1987), 17 C.C.E.L. 257 (B.C.C.A.) ; *Grenier v. Timmins Board of Education* , Ont. H.C., No. 1250/82, May 31, 1984, 26 A.C.W.S. (2d) 285 ; *Pettit v. Prince George & District Credit Union* (1991), 35 C.C.E.L. 140 (B.C.S.C.) ; and *Roy v. B.N.P.P. Regional Police Commission* (1986), 15 C.C.E.L. 167 (N.B.Q.B.) . Without question, the present factual situation is a novel one for this court.

33 Some have suggested that it is inappropriate to extend the application of *Hedley Byrne* , supra, to representations made by an employer to a prospective employee in the course of an interview because it places a heavy burden on employers. As will be apparent from my reasons herein, I disagree in principle with this view. However, I find it unnecessary for the purposes of this appeal to engage in a general and abstract discussion on the applicability of the tort of negligent misrepresentation to pre-employment representations. The thrust of the respondent's argument before this court is not that the appellant's action is unfounded in law. Rather, the respondent argues that the appellant has not made out a case for compensation based on negligent misrepresentation. Accordingly, this appeal may be disposed of simply by considering whether or not the required elements under the *Hedley Byrne* , supra, doctrine are established in the facts of this case. In my view, they are.

34 The required elements for a successful *Hedley Byrne* , supra, claim have been stated in many authorities, sometimes in varying forms. The decisions of this court cited above suggest five general requirements: (1) there must be a duty of care based on a "special relationship" between the representor and the representee; (2) the representation in question must be untrue, inaccurate, or misleading; (3) the representor must have acted negligently in making said misrepresentation; (4) the representee must have relied, in a reasonable manner, on said negligent misrepresentation; and (5) the reliance must have been detrimental to the representee in the sense that damages resulted. In the case at bar, the trial judge found that all elements were present and allowed the appellant's claim.

35 In particular, White J. found, as a fact, that the respondent's representative, Mr. Johnston, had misrepresented the nature and existence of the employment opportunity for which the appellant had applied, and that the appellant had relied to his detriment on those misrepresentations. These findings of fact were undisturbed by the Court of Appeal and, except for a few passing remarks, the respondent does not challenge them before this court. Thus, the second, fourth, and fifth requirements are not in question here.

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36 The only issues before this court deal with the duty of care owed to the appellant in the circumstances of this case and the alleged breach of this duty (i.e., the alleged negligence). The respondent concedes that a "special relationship" existed between itself (through its representative) and the appellant so as to give rise to a duty of care. However, it argues that this duty is negated by a disclaimer contained in the employment contract signed by the appellant more than two weeks after the interview. Furthermore, the respondent argues that any misrepresentations made during the hiring interview were not made in a negligent manner. For reasons that follow, it is my view that both submissions fail.

37 However, before turning to these issues, I intend to deal with a preliminary matter not directly raised in argument. This appeal was argued before this court in close proximity to the case *BG Checo International Ltd. v. British Columbia Hydro & Power Authority* , S.C.C., Nos. 21939 and 21955, January 21, 1993 [reported 75 B.C.L.R. (2d) 145]. That case involved circumstances somewhat similar to those in the present appeal in that it also dealt with a claim for damages based on an alleged negligent misrepresentation stem ming from pre-contractual negotiations. Generally speaking, in *BG Checo* as in the case at bar, it was argued that certain representations made in a pre-contractual setting did not correspond with the post-agreement reality and were made in a negligent manner. In both cases, the defendants relied on the contract signed by the parties subsequent to the alleged negligent misrepresentation in order to bar the plaintiffs' claim in tort. As my conclusion in *BG Checo* is opposite from the one I take herein, I believe it is useful at the outset to explain why this case is clearly distinguishable from *BG Checo* . In doing so, my hope is to clarify some of the confusion which currently exists with respect to pre-contractual negligent misrepresentations.

B. Preliminary Observations on the Effect of the Employment Agreement on this Appeal

38 As I stated in *BG Checo* , it is now clear that an action in tort for negligent misrepresentation may lie even though the relevant parties to the action (i.e., the representee/plaintiff and the representor/defendant) are in a contractual relationship: see *Esso Petroleum Co. v. Mardon,* [1976] 2 All E.R. 5 (C.A.) ; *Sodd Corp. v. Tessis* (1977), 17 O.R. (2d) 158 (C.A.) ; *Kingu v. Walmar Ventures Ltd.* (1986), 38 C.C.L.T. 51 (B.C.C.A.) ; *Carman Construction* , supra; *V.K. Mason Construction* , supra; *Rainbow Industrial Caterers* , supra; and L.N. Klar, *Tort Law* (1991), at p. 162, n. 89. More particularly, the fact that the alleged negligent misrepresentations are made in a pre-contractual setting, such as during negotiations or in the course of an employment hiring interview, and the fact that a contract is subsequently entered into by the parties do not, in themselves, bar an action in tort for damages caused by said misrepresentations: see, for example, *Esso Petroleum* , supra, and the cases cited above dealing specifically with pre-employment misrepresentation.

39 This is not to say that the contract in such a case is irrelevant and that a court should dispose of the plaintiff's tort claim independently of the contractual arrangement. On the contrary, depending on the circumstances, the subsequent contract may play a very important role in determining whether or not, and to what extent, a claim for negligent misrepresentation shall succeed. Indeed, as evidenced by my conclusion in *BG Checo* , such a contract can have the effect of negating the action in tort and of confining the plaintiff to whatever remedies are available under the law of contract. On the other hand, even if the tort claim is not barred altogether by the contract, the duty or liability of the defendant with respect to negligent misrepresentations may be limited or excluded by a term of the subsequent contract so as to diminish or extinguish the plaintiff's remedy in tort: see, for example, *Hedley Byrne* (although this case did not involve a con tract) and *Carman Construction* (although this case involved mostly post-contractual representations), supra. Equally true, however, is that there are cases where the subsequent contract will have no effect whatsoever on the plaintiff's claim for damages in tort. As will be apparent from these reasons, it is my view that the employment agreement signed by the appellant in March of 1983 is governed by this last proposition.

40 When considering the effect of the subsequent contract on the representee's tort action, everything revolves around the nature of the contractual obligations assumed by the parties and the nature of the alleged negligent misrepresentation. The first and foremost question should be whether there is a specific contractual duty created by an express term of the contract which is co-extensive with the common law duty of care which the representee alleges the representor has breached. Put another way, did the pre-contractual representation relied on by the plaintiff become an express term of the subsequent contract? If so, absent any overriding considerations arising from the context in which the transaction

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occurred, the plaintiff cannot bring a concurrent action in tort for negligent misrepresentation and is confined to whatever remedies are available under the law of contract. The authorities supporting this proposition, including the decision of this court in *Central Trust Co. v. Rafuse*, [1986] 2 S.C.R. 147 , are fully canvassed in my reasons in *BG Checo* . As alluded to in *BG Checo* , this principle is an exception to the general rule of concurrency espoused by this court in *Central Trust v. Rafuse* , supra.

41 There lies, in my view, the fundamental difference between the present appeal and *BG Checo* , supra. In the latter case, the alleged pre-contractual misrepresentation had been incorporated verbatim as an express term of the subsequent contract. As such, the common law duty of care relied on by the plaintiff in its tort action was co-extensive with a duty imposed on the defendant in contract by an express term of their agreement. Thus, it was my view that the plaintiff was barred from exercising a concurrent action in tort for the alleged breach of said duty, and this view was reinforced by the commercial context in which the transaction occurred. In the case at bar, however, there is no such concurrency. The employment agreement signed by the appellant in March of 1983 does not contain any express contractual obligation co-extensive with the duty of care the respondent is alleged to have breached. The provisions most relevant to this appeal (clauses 13 and 14) contain contractual duties clearly different from, not co-extensive with, the common law duty invoked by the appellant in his tort action.

42 Had the appellant's action been based on pre-contractual representations concerning the length of his involvement on the Multiview project or his "job security", as characterized by the Court of Appeal, the concurrency question might be resolved differently in light of the termination and reassignment provisions of the contract. However, it is clear that the appellant's claim was *not* that Mr. Johnston negligently misrepresented the amount of time he would be working on Multiview or the conditions under which his employment could be terminated. In other words, he did not argue that the respondent, through its representative, breached a common law duty of care by negligently misrepresenting his security of employment with Cognos. Rather, the appellant argued that Mr. Johnston negligently misrepresented the nature and existence of the employment opportunity being offered. It is the existence, or reality, of the job being interviewed for, not the extent of the appellant's involvement therein, which is at the heart of this tort action. A close reading of the employment agreement reveals that it contains no express provisions dealing with the respondent's obligations with respect to the nature and existence of the Multiview project. Accordingly, the ratio decidendi of my reasons in *BG Checo* is inapplicable to the present appeal. While both cases involve pre-contractual negligent misrepresentations, only *BG Checo* involved an impermissible concurrent liability in tort and contract; an exception to the general rule of concurrency set out in *Central Trust v. Rafuse* , supra. The case at bar does not involve concurrency at all, let alone an exception thereto.

43 Having said this, it does not follow that the employment agreement is irrelevant to the disposition of this appeal. As I mentioned earlier, even if the tort claim is not barred altogether by the contract as in *BG Checo* , the duty or liability of the representor in tort may be limited or excluded by a term of the subsequent contract. In this respect, the respondent submits that the Court of Appeal was correct in finding that clauses 13 and 14 of the employment agreement represent a valid disclaimer for the misrepresentations allegedly made during the hiring interview, thereby negating any duty of care. I shall return to this issue in the last part of my reasons. I prefer to deal next with the questions of whether the respondent or its representative owed a duty of care to the appellant during the pre-employment interview and, if so, whether there was a breach of this duty in all the circumstances of this case.

C. The Duty of Care Owed to the Appellant

44 The respondent concedes that it itself and its representative, Mr. Johnston, owed a duty of care towards the six job applicants being interviewed, including the appellant, not to make negligent misrepresentations as to Cognos and the nature and permanence of the job being offered. In so doing, it accepts as correct the findings of both the trial judge and the Court of Appeal that there existed between the parties a "special relationship" within the meaning of *Hedley Byrne* , supra.

45 In my view, this concession is a sensible one. Without a doubt, when all the circumstances of this case are taken into account, the respondent and Mr. Johnston were under an obligation to exercise due diligence throughout the hiring

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interview with respect to the representations made to the appellant about Cognos and the nature and existence of the employment opportunity.

46 There is some debate in academic circles, fuelled by various judicial pronouncements, about the proper test that should be applied to determine when a "special relationship" exists between the representor and the representee which will give rise to a duty of care. Some have suggested that "foreseeable and reasonable reliance" on the representations is the key element to the analysis, while others speak of "voluntary assumption of responsibility" on the part of the representor. Recently, in *Caparo Industries plc v. Dickman*, [1990] 1 All E.R. 568 (H.L.) , a case unlike the present one in that there the whole issue revolved around the existence of a duty of care, the House of Lords suggested that three criteria determine the imposition of a duty of care: foreseeability of damage; proximity of relationship; and the reasonableness or otherwise of imposing a duty.

47 For my part, I find it unnecessary — and unwise in view of the respondent's concession — to take part in this debate. Regardless of the test applied, the result which the circumstances of this case dictate would be the same. It was foreseeable that the appellant would be relying on the information given during the hiring interview in order to make his career decision. It was reasonable for the appellant to rely on said representations. There is nothing before this court that suggests that the respondent was not, at the time of the interview or shortly thereafter, assuming responsibility for what was being represented to the appellant by Mr. Johnston. As noted by the trial judge, Mr. Johnston discussed the Multiview project in an unqualified manner, without making any relevant caveats. The alleged disclaimers of responsibility are provisions of a contract signed more than two weeks after the interview. For reasons that I give in the last part of this analysis, these provisions are not valid disclaimers. They do not negate the duty of care owed to the appellant or prevent it from arising as in *Hedley Byrne* and *Carman Construction* , supra. It was foreseeable to the respondent and its representative that the appellant would sustain damages should the representations relied on prove to be false and negligently made. There was, undoubtedly, a relationship of proximity between the parties at all material times. Finally, it is not unreasonable to impose a duty of care in all the circumstances of this case; quite the contrary, it would be unreasonable *not* to impose such a duty. In short, therefore, there existed between the parties a "special relationship" at the time of the interview. The respondent and its representative Mr. Johnston were under a duty of care during the pre-employment interview to exercise reasonable care and diligence in making representations as to the employer and the employment opportunity being offered.

48 Although it was not argued before this court, I wish to add what is implicit in my acceptance of the respondent's concession, namely, that I reject the so-called restrictive approach as to who can owe a *Hedley Byrne* , supra, duty of care, often associated with the majority judgment in *Mutual Life & Citizens' Assurance Co. v. Evatt*. [1971] A.C. 793 (P.C.) . In my opinion, confining this duty of care to "professionals" who are in the business of providing information and advice such as doctors, lawyers, bankers, architects, and engineers, reflects an overly simplistic view of the analysis required in cases such as the present one. The question of whether a duty of care with respect to representations exists depends on a number of considerations including, but not limited to, the representor's profession. While this factor may provide a good indication as to whether a "special relationship" exists between the parties, it should not be treated in all cases as a threshold requirement. There may be situations where the surrounding circumstances provide sufficient indicia of a duty of care, notwithstanding the representor's profession. Indeed, the case at bar is a good example. I find support for a more flexible approach on this question in a number of authorities: see, for example, the dissenting reasons of Lord Reid and Lord Morris in *Mutual Life* , supra; *Esso Petroleum* , supra; *Howard Marine & Dredging Co. v. A. Ogden & Sons (Excavations) Ltd.*, [1978] Q.B. 574 (C.A.) ; *L. Shaddock & Associates Pty. Ltd. v. Parramatta City Council* (1981), 150 C.L.R. 225 (Aust. H.C.) ; *Blair v. Canada Trust Co.* (1986), 38 C.C.L.T. 300 (B.C.S.C.) ; *Nelson Lumber Co. v. Koch* (1980), 13 C.C.L.T. 201 (Sask. C.A.) ; and A.M. Linden, *Canadian Tort Law* (4th ed., 1988), at pp. 400-404.

D. The Breach of the Duty of Care

(1) Introduction

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49 The next issue deals with whether the above duty of care was breached during the course of the pre-employment interview of February 14, 1983. The main question to be addressed here is whether the misrepresentations of Mr. Johnston during the interview were negligently made, as found by the trial judge.

50 In order to answer this question, it will be necessary to determine the nature and extent of the duty of care owed to the appellant in the circumstances of this case or, as I prefer to characterize it, the standard of care imposed by law on the respondent and its representative. Specifically, we must ask ourselves whether it is sufficient, in law, that Mr. Johnston was truthful during the interview and that he believed in what he was representing, as found by the Court of Appeal, or whether something more was required of him?

51 I will also deal under this heading with a sub-issue raised by the respondent, namely, the nature of the misrepresentations made in the case at bar. As previously noted, the trial judge found as a fact that some of the representations made to the appellant in the course of the pre-employment interview were misrepresentations in the sense that they were inaccurate or misleading. This finding, made on the basis of White J.'s assessment of all the evidence, was not disturbed in any way by the Court of Appeal. The respondent is not challenging — at least not directly — this finding of fact before this court. However, it is arguing that regardless of any negligence these misrepresentations are not actionable at law under the *Hedley Byrne* , supra, principle because they depend on inferences or implications rather than on direct and express statements, and because they relate to a future expectation. I shall address this submission following my review of the relevant standard of care and of its application to the facts of this case.

(2) The Standard of Care Imposed on the Respondent

52 According to Finlayson J.A., the duty imposed on the respondent and its representative is "no more than a duty to take care that the representations made were responsible and accurate to the knowledge of Johnston and of his principal, Cognos" (p. 186). In his view, Mr. Johnston was not obliged to go further than he did in describing the employment opportunity to the appellant: "What he said was truthful, he believed in it, that was enough" (p. 188).

53 Before this court, the respondent adopts the position of Finlayson J.A. with respect to the applicable standard of care. It also adopts his finding that the trial judge erred in imposing a higher standard than was required in the circumstances, namely, a standard of disclosure to the appellant concerning the extent of the respondent's financial commitment to the Multiview project. It is submitted that the trial judge's approach is an unwarranted extension to the law of master/servant of a quasi-fiduciary duty of uberrima fides. Finally, the respondent adopts the finding of Finlayson J.A. that the duty of care imposed on the respondent and its representative was fully discharged. In this respect, the respondent emphasizes the fact that the recruitment process for the position in question had been commenced by Mr. Johnston with full knowledge and support of a number of senior executives of the respondent, and that there was in fact a "commitment" of the respondent to develop Multiview in the way out lined by Mr. Johnston during the interview.

54 The appellant characterizes the applicable standard of care in a somewhat different manner. He submits that the respondent's duty of care required that both it itself and Mr. Johnston take reasonable steps to avoid conveying information to the appellant about his prospective employment that was materially inaccurate or misleading. According to him, this duty also required them to put themselves "in the appellant's shoes" in assessing the possible impact of their representations on his career choices. In particular, it is argued that they had a duty to consider what inferences the appellant would probably make from the pre-employment statements. The appellant concedes that this standard appears to be high; however, he submits that it is justified in a pre-employment situation based on a number of "policy considerations". Finally, the appellant argues that the applicable standard requires not only that an employer provide accurate information regarding the employment opportunity, but it also requires that he or she provide complete information; viz., full disclosure. In the case at bar, the appellant submits that the duty of care was not discharged since the information provided by Mr. Johnston was incomplete; there was no mention of the absence of a financial commitment. In any event, it is submitted that there was negligence even under a lower standard of care because the respondent and its representative did not ensure that the information provided, both expressly and impliedly, was accurate.

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55 In my view, the relevant standard of care is neither the one advanced by the respondent and the Court of Appeal nor the one proposed by the appellant. The former is too low as it equates, in essence, a duty of care with a duty of common honesty. On the other hand, the standard of care proposed by the appellant is too onerous as it is tantamount to requiring full disclosure from employers during pre-employment interviews. This court has been presented with no compelling reasons to treat representations made in an employment context differently from representations made in any other context. It is unfortunate that the appellant has spent considerable time in his argument trying to convince this court to recognize a fundamentally new standard of care, specific to the employment context. Clearly, the standard of care normally required by law is sufficient to dispose of this appeal in the appellant's favour. Upholding the trial judge's finding of negligence does not require an expansion of tort law into previously uncharted and hence unknown waters. Rather, it simply requires an application of well established principles of the law of negligence.

56 The applicable standard of care should be the one used in every negligence case namely the universally accepted, albeit hypothetical, "reasonable person". The standard of care required by a person making representations is an objective one. It is a duty to exercise such reasonable care as the circumstances require to ensure that representations made are accurate and not misleading: see *Hedley Byrne* , supra, at p. 486, per Lord Reid; *Hodgins v. Nepean Hydro-Electric Commission* , supra, at pp. 506-9, per Ritchie J. for the majority of this court; *Wooldridge v. H.B. Nickerson & Sons* , supra, at pp. 135-36; J.G. Fleming, *The Law of Torts* (7th ed., 1987), at pp. 96-104 and 614; Linden, supra, at pp. 105-19; and Klar, supra, at pp. 159-60. Professor Klar provides some useful insight on this issue (at p. 160):

> An advisor does not guarantee the accuracy of the statement made, but is only required to exercise reasonable care with respect to it. As with the issue of standard of care in negligence in general, this is a question of fact which must be determined according to the circumstances of the case. Taking into account the nature of the occasion, the purpose for which the statement was made, the foreseeable use of the statement, the probable damage which will result from an inaccurate statement, the status of the advisor and the level of competence generally observed by others similarly placed, the trier of fact will determine whether the advisor was negligent.

57 In my opinion, the trial judge did not depart from the applicable standard of care in rendering his decision. He found that, "in all the circumstances", the misrepresentations made by the respondent's representative were negligently made. Unlike the Court of Appeal, I find no reason to interfere with his careful and considered finding on this point.

58 As I see it, the Court of Appeal erred in two important respecta when it interfered with White J.'s finding of negligence. First, it mischaracterized his reasons on the negligence issue. Finlayson J.A. said the following (at p. 187):

> The trial judge found that [Mr. Johnston] had a duty to go further and to point out the details of the internal decision-making process at Cognos and stress that the process had not been completed. In other words, his own *bona fide* belief as a knowledgeable executive that the program was going forward was not sufficient. He had to divulge to all of the applicants that he interviewed the precise status of the corporate commitment to the development of the new product so that they could make their own assessment of the viability of the project.
>
> In my opinion, this casts the duty too high. It suggests that at least a quasi-fiduciary relationship existed between corporation and job applicant, giving rise to a duty to make full disclosure.

59 Unlike Finlayson J.A., I do not read the trial judge's reasons as suggesting that the respondent and its representative had a *duty to make "full disclosure"* in the sense described above, and that the respondent was liable for a failure to meet this duty. Rather, I read his reasons as suggesting that, in all the circumstances of this case, Mr. Johnston breached a *duty to exercise reasonable care* by, inter alia, representing the employment opportunity in the way he did without, at the same time, informing the appellant about the precarious nature of the respondent's financial commitment to the development of Multiview. In reality, the trial judge did not impose a duty to make full disclosure on the respondent and its representative. He simply imposed a duty of care, the respect of which required, among other things and in the

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circumstances of this case, that the appellant be given highly relevant information about the nature and existence of the employment opportunity for which he had applied.

60 There are many reported cases in which a failure to divulge highly relevant information is a pertinent consideration in determining whether a misrepresentation was negligently made: see, for example, *Fine's Flowers Ltd. v. General Accident Assurance Co.* (1974), 5 O.R. (2d) 137 (H.C.) , at p. 147, affirmed (1977), 17 O.R. (2d) 529 (C.A.) ; *Grenier v. Timmins Board of Education* , supra; *Wooldridge v. H.B. Nickerson & Sons* , supra; *Hendrick v. De Marsh* (1984), 45 O.R. (2d) 463 (H.C.) , affirmed on other grounds (1986), 54 O.R. (2d) 185 (C.A.) ; *Steer v. Aerovox* , supra; *W.B. Anderson & Sons Ltd. v. Rhodes (Liverpool) Ltd.*, [1967] 2 All E.R. 850 (Liverpool Assizes) ; and *V.K. Mason Construction* , supra. In the last case, Wilson J. said the following speaking for this court (at p. 284):

> The statement was negligent because it was made without revealing that the Bank was giving an assurance based solely on a loan arrangement which Mason had already said was insufficient assurance to it of the existence of adequate financing.

In so doing, these cases and the trial judgment in the case at bar are not applying a standard of uberrima fides to the transactions involved therein. Quite frankly, this notion is irrelevant to a determination of whether the representor has breached a common law duty of care in tort. These decisions simply reflect the applicable law by taking into account all relevant circumstances in deciding whether the representor's conduct was negligent. In some cases, this includes the failure to divulge highly pertinent information.

61 The second error made by the Court of Appeal is that it substituted for the "higher" standard of care allegedly imposed by the trial judge, a standard well below the one required by law. Once again, it is worth repeating the final words of Finlayson J.A. on the negligence issue: "Johnston was not obliged to go farther than he did in describing the job prospects. What he said was truthful, he believed in it, that was enough" (p. 188). In essence, the Court of Appeal reduced a common law duty of care to a duty of common honesty. Undoubtedly, the latter duty existed in the case at bar, as it exists during any pre-contractual negotiations.

62 However, the duty of care owed by a representor to a representee, *when there exists a "special relationship" within the meaning of Hedley Byrne, supra* , is distinct in nature and scope from a duty to be honest and truthful. As was stated in *Hedley Byrne* , supra, by Lord Morris (at pp. 502-3):

> Independently of contract, there may be circumstances where information is given or where advice is given which establishes a relationship which creates a duty not only to be honest but also to be careful.
>
> .....
>
> In these circumstances, I think some duty towards the unnamed person, whoever it was, was owed by the bank. There was a duty of honesty. The great question, however, is whether there was a duty of care.

and by Lord Pearce (at p. 539):

> There is also, in my opinion, a duty of care created by special relationships which, though not fiduciary, give rise to an assumption that care as well as honesty is demanded.

See also *Hayward v. Mellick* (1984), 45 O.R. (2d) 110 (C.A.) , and *Carman Construction* , supra, at p. 973.

63 A duty of care with respect to representations made during pre-contractual negotiations is over and above a duty to be honest in making those representations. It requires not just that the representor be truthful and honest in his or her representations. It also requires that the representor exercise such reasonable care as the circumstances require to ensure that the representations made are accurate and not misleading.

64 Although the representor's subjective belief in the accuracy of the representations and his moral blameworthiness, or lack thereof, is highly relevant when considering whether or not a misrepresentation was fraudulently made, it serves

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little, if any, purpose in an inquiry into negligence. As noted above, the applicable standard of care is that of the objective reasonable person. The representor's belief in the truth of his or her representations is irrelevant to that standard of care. The position adopted by the Court of Appeal seems to absolve those who make negligent misrepresentations from liability if they believe that their representations are true. Such a position would virtually eliminate liability for negligent misrepresentation as liability would result only where there is actual knowledge that the representation made is not true; the basis of *fraudulent* misrepresentation. In essence, the Court of Appeal has returned to the pre-*Hedley Byrne* , supra, state of law where a misrepresentation had to be accompanied by moral blameworthiness in order to support an action in tort for damages: see, in this respect, my discussion in *BG Checo* , supra, of the context in which *Hedley Byrne* was decided. The question facing the trial judge on the negligence issue was not whether Mr. Johnston was truthful or believed in what he was representing to the appellant. The question was whether he exercised such reasonable care as the circumstances required so as to ensure the accuracy of his representations.

65 The trial judge found that the respondent's representative had acted negligently in making the misrepresentations to the appellant about the nature and existence of the employment opportunity and, in particular, the extent of the respondent's commitment to the Multiview project. He found that Mr. Johnston was aware, based upon his expertise in the field of computer development, that until there was a feasibility study in which cost estimates had been submitted, considered, and approved by senior management, one could not say that the respondent had made a firm commitment to the project as Mr. Johnston envisaged it and as he described it to the appellant in the interview.

66 As noted above, the trial judge also made the following important findings: Mr. Johnston knew, or ought to have known, that the truth of his representations depended on the approval by the corporate management team of the cost estimates he had prepared for the research and development of the Multiview project; it is reasonable to infer that Mr. Johnston, at the time of the interview, contemplated that the budgetary needs for the Multiview project would be substantial and that approval was at best speculative; Mr. Johnston must have been aware of the continued poor sales performance of the Multiview product line; Mr. Johnston did not disclose to the appellant that senior management had not yet given the financial commitment required to make the plans for the Multiview project a probable reality; Mr. Johnston's expertise in the computer development field should have made him aware that, notwithstanding his conversations with senior management and the meeting of December 21, 1982, there was still a considerable risk that senior management would not give budgetary approval to his plans; Mr. Johnston knew that the appellant was relying on the information he was providing during the interview; Mr. Johnston knew that the appellant had a secure, responsible, and well-paying position as a chartered accountant in Calgary and that coming to Ottawa would involve moving himself and his family across the country; and Mr. Johnston was aware that the appellant was relying on the position with Cognos to enhance his career significantly as an accountant.

67 These findings are fully supported by the evidence adduced at trial. I see no reason to interfere with the trial judge's conclusion that the misrepresentations made to the appellant were, in all the circumstances, "negligent misrepresentations". Under the standard of care described above, Mr. Johnston failed to exercise such reasonable care as the circumstances required him to in making the representations he did during the interview. Particularly, he should not have led the appellant to believe that the Multiview project as described during the interview was a reality when, in fact, he knew very well that the most important factor to the existence of the project, as he was describing it, was financial support by the respondent.

68 Before this court, the respondent made extensive reference to the evidence adduced at trial to indicate that it did, in reality, plan to develop Multiview and to make it a profitable project. While it seems to be true that Cognos was "committed" to the project at the end of 1982 and early 1983, it was not committed in the most crucial respect, namely funding. As found by the trial judge, the impression given during the interview was not consistent with the fundamental reality that funding for the project was not yet approved.

69 In the end, I am unable to find any ground for interfering with White J.'s finding of negligence. There was, in the circumstances of this case, a breach of the duty of care owed to the appellant. In light of this conclusion, it is unnecessary to determine whether, as argued by the appellant, other members of the respondent such as senior management were

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negligent on the facts of this case. Mr. Johnston's conduct during the interview is sufficient to support a finding of liability against the respondent.

(3) The Nature of the Misrepresentations

70 The respondent takes the alternate position that, even accepting the trial judge's findings of misrepresentations and of negligence, the appellant's action must fail because the representations relied on are not actionable under the *Hedley Byrne* , supra, doctrine. In this respect, the respondent argues that the representations depend on inferences or implications, rather than on direct statements, and also relate to a future expectation. The appellant makes no submissions on this point. It is unclear whether this submission of the respondent was advanced prior to the appeal to this court. If so, it has received very little attention by the courts below. There is only a brief discussion, and rejection, of the "future expectation" aspect of the argument in the trial judge's reasons and the Court of Appeal makes no reference whatsoever to this submission.

71 In my view, the respondent's alternate position cannot succeed in the circumstances of this case. First of all, I reject as incorrect the suggestion that the representations in question relate solely to future events or expectations. I reproduce again, for convenience, a passage from White J.'s judgment in which he finds, as a fact, that misrepresentations were made to the appellant in the hiring interview (at pp. 415-16):

> The effect of these misrepresentations was that the [appellant] would have a position in the research and development of the product "Multiview"; that that position would be a significant one and would involve his expertise as an accountant; that he would perform the responsible role of seeing to proper accounting standards being implemented into the product; that beyond the three modules immediately in contemplation were a minimum of four other modules; and that the project of "Multiview", in connection with which [the appellant] would be hired would last a minimum of two years. I find further that Mr. Johnston implicitly represented that management had made a firm budgetary commitment to the development of four other modules in addition to those then presently under development.

72 Obviously, some aspects of the misrepresentations made to the appellant about the employment opportunity were, by their very nature, matters in futuro. Statements about the appellant's involvement with the respondent and his responsibilities should he be offered a position are representations that relate to future conduct and events. There are authorities supporting the view that only representations of existing facts, and not those relating to future occurrences, can give rise to actionable negligence: see, for example, *Williams v. Saanich School District No. 63* (B.C.S.C.), supra; *Datile Financial Corp. v. Royal Trust Corp. of Canada* (1991), 5 O.R. (3d) 358 (Gen. Div.) ; *Foster Advertising Ltd. v. Keenberg* (1987), 38 C.C.L.T. 309 (Man. C.A.) ; and *Andronyk v. Williams* (1985), 35 C.C.L.T. 38 (Man. C.A.) .

73 However, assuming without deciding that this view of the law is correct, the representations most relevant to the appellant's action are *not* those relating to his future involvement and responsibilities with Cognos, but those relating to the very existence of the job for which he had applied. That is a matter of existing fact. It was implicitly represented that the job applied for did in fact, *at the time of the interview* , exist in the manner described by Mr. Johnston. As found by the trial judge, however, such was not the case. The employment opportunity described to the appellant was not, at the time of the interview, a fait accompli for the respondent. Clearly, this misrepresentation relates to facts presumed to have existed at the time of the interview: the respondent's financial commitment to the development of Multiview and the existence of the employment opportunity offered. It is *not* a "remark by a defendant concerning the outcome of a future event" (*Williams v. Saanich School District No. 63* (B.C.S.C.), supra, at p. 240), a "representation as to future occurrences" (*Datile Financial Corp. v. Royal Trust* , supra, at p. 379), a "statement of intention or forecast of the future" (*Foster Advertising Ltd. v. Keenberg* , supra, at p. 325), or "forecasting" (*Andronyk v. Williams* , supra, at p. 57).

74 The other aspect of the respondent's argument is that representations which depend on implications or inferences cannot give rise to actionable negligence under the *Hedley Byrne* , supra, doctrine. Again, I reject this submission.

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However, on this issue, I prefer, for obvious reasons, to challenge the principle advanced by the respondent rather than simply reject its application to the facts of this case.

75 In my view, there is no compelling reason in principle, authority, or policy for the proposition that, as a general rule, an implied representation cannot under any circumstance give rise to actionable negligence. The only authority offered by the respondent is the decision of the New South Wales Court of Appeal in *Minister Administering the Environmental Planning and Assessment Act, 1979 v. San Sebastian Pty. Ltd.*, [1983] 2 N.S.W.L.R. 268 , affirmed on other grounds (1986), 68 A.L.R. 161 (H.C.), applied by Southin J.A. of the British Columbia Court of Appeal, in dissent, in *BG Checo International Ltd. v. British Columbia Hydro & Power Authority* (1990), 44 B.C.L.R. (2d) 145 . The reasons of Mahoney and Hutley JJ.A. in the former case appear indeed to support the proposition that nothing less than an express, or tantamount to an express, representation can suffice under the *Hedley Byrne* , supra, doctrine. It is not without significance, however, that the High Court of Australia in dismissing a subsequent appeal on different grounds expressly refrained from making any comments on this issue. Rather, the majority of the court preferred to base its judgment, inter alia, on the fact that no misrepresentations, whether "express or implied", had been made. In other words, the High Court found nothing misleading or inaccurate in what was represented, regardless of how the representation was characterized.

76 On the other hand, there is considerable authority for the more flexible view that, *in appropriate circumstances* , implied misrepresentations can, and often do, give rise to actionable negligence: see, for example, *Banque Financière de la Cité SA v. Westgate Insurance Co.*, [1989] 2 All E.R. 952 (C.A.) , at p. 1000, affirmed on other grounds [1990] 2 All E.R. 947 (H.L.) ; *Datile Financial Corp. v. Royal Trust* , supra, at p. 379; *Hendrick v. De Marsh* (Ont. H.C.), supra; *Steer v. Aerovox* , supra; and *Doherty v. Allen* (1988), 55 D.L.R. (4th) 746 (N.B.C.A.) .

77 In my opinion, a flexible approach to this issue is preferable. It is arbitrary and premature to declare as a general rule that nothing less than express or direct representations can succeed under the *Hedley Byrne* , supra, doctrine. Undoubtedly, there will be cases such as the present one where the surrounding circumstances are such that it makes little difference, if any, how one characterizes the manner in which the representation is made, and where it would be unjust to deny recovery simply because the representation relied on is said to be implied rather than express. It is unnecessary for me to set out in detail the circumstances in which so-called implied representations can be enough to sustain an action in tort for negligent misrepresentation. I prefer leaving this task to trial judges dealing with specific factual situations. Suffice it to say that the case at bar falls well within this category.

78 There was a considerable number of express representations made by Mr. Johnston during the interview which point directly towards the existence of the Multiview project and the nature of the respondent's commitment thereto. The implied misrepresentation found by the trial judge is not only reasonable in the surrounding circumstances, but it is also perhaps the only inference that could be drawn from the direct representations made to the appellant during the interview. A reasonable person placed in the appellant's position would, without a doubt, have drawn the same inference from what was being said that the appellant and trial judge did.

79 This is not a situation where many different and conflicting interpretations may reasonably be drawn from a series of direct representations and where the representee advances the implied meaning most favourable to recovery. This is a case where everything said and represented during the interview points to the same conclusion: the Multiview project as described by Mr. Johnston was a reality in that the respondent had given its financial support to its development. The appellant had a relatively secure and well paying job in Calgary and, as found by the trial judge, he would not have chosen to move across the country if he thought there was a substantial risk that the employment opportunity described to him would no longer exist, after his arrival in Ottawa. To a large extent, this risk was alleviated by the representations made during the interview. For these reasons, the fact that the representation in question falls short of being express should not, in the circumstances of this case, preclude the appellant from relying on the *Hedley Byrne* , supra, doctrine and from obtaining a remedy for the damages he suffered.

E. The Employment Agreement Signed Subsequent to the Negligent Misrepresentations

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80 Thus far, I have stated that the courts below were correct in finding a "special relationship" between the parties as to give rise to a duty of care during the interview, and that the misrepresentations found by the trial judge were indeed made in a negligent manner in all the circumstances of the case. Again, there is no question in this appeal that the appellant reasonably relied, to his detriment, on these negligent misrepresentations. The only remaining issue is whether the employment agreement signed by the appellant more than two weeks after the interview affects, in any way, the above findings or the consequence that would normally follow therefrom, namely, liability of the respondent for the damages caused to the appellant.

81 Finlayson J.A. found that clauses 13 and 14 of the employment agreement constituted an adequate, albeit not express, "disclaimer of responsibility" for the representations made during the interview because these clauses contradicted or were inconsistent with those representations. The respondent adopts this conclusion, submitting that there is a clear inconsistency between the contract and the alleged misrepresentations and that this inconsistency is sufficient to constitute a disclaimer within the meaning of *Hedley Byrne* , supra. The respondent argues that the representation relied on by the appellant goes to the issue of job security and that the contract of employment specifically addresses, and contradicts, this issue in its provisions dealing with reassignment and termination of employment, "without cause", on one month's notice. Furthermore, the respondent relies on the decision of this court in *J. Nunes Diamonds* , supra, for the proposition that the doctrine of *Hedley Byrne* , supra, "is inapplicable to any case where the relationship between the parties is governed by a contract, unless the negligence relied on can properly be considered as 'an independent tort' unconnected with the performance of that contract". It is argued that the tort in question is not "independent" from the contract. Moreover, the respondent submits that the one month termination clause in the contract amounts to a "limitation of liability clause" and that the appellant is attempting to circumvent this clause by its present action in tort, contrary to the decision of this court in *Central Trust v. Rafuse* , supra. Finally, the respondent argues that the appellant's conduct after his arrival at the company and his learning of the developments regarding the Multiview project amounts to an affirmation of his contract of employment.

82 For his part, the appellant submits that the tort at issue is "independent" of the employment agreement within the meaning of *J. Nunes Diamonds* , supra, and is not affected in any way by its provisions. In particular, it is submitted that clauses 13 and 14 of the employment contract do not amount to a valid disclaimer and have no bearing whatsoever on the respondent's liability in tort. In this respect, he argues that express contractual terms are required in order to negate an otherwise "independent" duty of care. Furthermore, the appellant claims he was simply attempting to mitigate his damages by staying with the respondent after the reassignments. According to him, any "affirmation" of the contract is irrelevant since the tort in issue is "independent" from the contract and because the damages crystallized at the moment he became aware of the misrepresentations.

83 As I see the matter, the specific employment agreement signed by the appellant is, in the circumstances of this case, irrelevant to his action for negligent misrepresentation. This contract falls within the third proposition suggested earlier in which a representee's claim for damages for a negligent pre-contractual misrepresentation is not affected, in any way, by the subsequent contract. I observed at p. 25 [paras. 38-40] of these reasons that this appeal is clearly distinguishable from *BG Checo* , supra, in that the common law duty of care relied on by the appellant is *not* , unlike in *BG Checo* , co-extensive with a duty imposed on the respondent by an express term of the employment agreement. This conclusion, in effect, disposes of the respondent's argument based on *J. Nunes Diamonds* , supra.

84 Indeed, as I alluded to in *BG Checo* , the aspect of the judgment of the majority in *J. Nunes Diamonds* , supra, upon which the respondent relies (the passage found at pp. 777-78) was qualified by the unanimousjudgment of this court in *Central Trust v. Rafuse* , supra, recognizing concurrency between contract and tort as a general rule subject to certain "exceptions", including (at p. 205):

> 2. What is undertaken by the contract will indicate the nature of the relationship that gives rise to the common law duty of care, but the nature and scope of the duty of care that is asserted as the foundation of the tortious liability must not depend on specific obligations or duties created by the express terms of the contract. *It is in that sense*

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> *that the common law duty of care must be independent of the contract* . The distinction, in so far as the terms of the contract are concerned, is, broadly speaking, between what is to be done and how it is to be done. A claim cannot be said to be in tort if it depends for the nature and scope of the asserted duty of care on the manner in which an obligation or duty has been expressly and specifically defined by a contract. [Emphasis added.]

Unlike in *BG Checo* , the common law duty of care invoked by the appellant *is* , for reasons already given, "independent" of the employment agreement. I would therefore reject this part of the respondent's argument which attempts to disallow the appellant's action in tort and to confine him to whatever remedies are available under the law of contract.

85 This leaves the question of whether the duty or liability of the respondent in tort is limited or excluded by a term of the employment agreement. As I see the matter, neither the respondent's duty of care nor its liability is affected by the terms of the employment agreement. For convenience, I reproduce again the provisions of this contract which play a determining role according to the Court of Appeal and the respondent:

> **Transfer**
>
>> 13. Quasar Systems reserves the right to reassign you to another position with the Company without reduction of your salary or benefits and upon one month's notice to you. Should such reassignment require your permanent relocation to another city, the Company will reimburse you for your expenses in accordance with the then current relocation policy.
>
> **Termination Notice — One Month**
>
>> 14. This Agreement may be terminated at any time and without cause by Quasar Systems Ltd. or by you. In the event of termination, Quasar Systems Ltd. will give you one month's notice of termination plus any additional notice that may be required by any applicable legislation. Similarly, you shall give Quasar Systems Ltd. one month's notice if you voluntarily terminate this Agreement. Quasar Systems Ltd. may pay you one month's salary in lieu of the aforesaid notice in which event this Agreement and your employment will be terminated on the date such payment in lieu of notice is made.

In my view, the Court of Appeal erred in giving to clauses 13 and 14 the effect of a "disclaimer of responsibility" within the meaning of *Hedley Byrne* and *Carman Construction* , supra. These provisions are clearly distinguishable from the disclaimers at issue in both *Hedley Byrne* and *Carman Construction* .

86 In *Hedley Byrne* , supra, the representee's bank requested certain financial information from the representors, merchant bankers for a potential client of the representee, "in confidence and without responsibility" on the part of the representors. The latter replied to the inquiry, in part, as follows: "Confidential. For your private use and without responsibility on the part of the bank or its officials." Unlike the present appeal, there was never any contractual relationship between the representee and the representor in *Hedley Byrne* . The House of Lords unanimously held that even though a duty of care with respect to representations could, in appropriate circumstances, exist, such a duty could not arise in *Hedley Byrne* since the representors had manifestly expressed, prior to the representations and to the knowledge of the representee, that they did not assume or accept responsibility for any of the information given.

87 *Carman Construction* , supra, on the other hand, concerned a misrepresentation made in a contractual setting. The corresponding clause in that case (cl.3.1) expressly provided that the plaintiff was not relying on the representations of the defendant: "the Contractor does not rely upon any information given or statement made to him in relation to the work by the Company" (p.961). The pertinent com ments of Martland J., writing for a unanimous court, are worth quoting (at pp. 972-73):

> In the *Hedley Byrne* case the decision was that the disclaimer of responsibility for the persons alleged to be liable for negligent misrepresentation, communicated to the other party, excluded the assumption of a duty of care. I regard the wording of clause 3.1 of the agreement as having the like effect. The judgment at trial dealt with the situation on

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> the basis that negligent misrepresentation had been established, but that clause 3.1 was an exemption clause which exempted C.P.R. from liability. In the circumstances of this case, I would prefer to regard the clause as establishing that C.P.R. did not assume any duty of care, and a claim in negligence will not arise in the absence of a duty of care.
>
> I reach this conclusion in the light of the facts to which I have already referred in dealing with the issue of collateral warranty. *Carman was made aware, when Fielding received the tender documents, and read and understood clause 3.1, that if it entered into an agreement with C.P.R. it was doing so on its own knowledge as to the quantities of material to be removed and that it would not rely upon any information or statement made to it by C.P.R. in relation to the work. Fielding was aware of this when he sought information from a C.P.R. employee. He knew that if information was obtained, Carman would be relying upon it at its own risk. In my opinion, on the facts of this case, a duty of care on the part of C.P.R. in respect of information provided by its employee never arose provided the information was given honestly* . The trial judge has found that the misrepresentation made to Carman was made innocently without intent to defraud. [Emphasis added.]

88 Also instructive is the following excerpt from the reasons of Wilson J.A. (as she then was), writing for the majority of the Court of Appeal, in *Carman Construction* ((1981), 33 O.R. (2d) 472 , at p. 473):

> This is not, in the view of the majority, a case in which, after making a negligent misrepresentation to the plaintiff in order to induce it to enter into a contract, the terms of which were at the time of the misrepresentation unknown, the defendant thereafter inserts into the contract an exculpatory clause in order to insulate itself against antecedent tort liability. This is a case in which the plaintiff tendered knowing that in the very contract on which it was tendering it had agreed to assume the risk of using any information obtained by it from the defendant's employees.

89 Contrary to *Hedley Byrne* and *Carman Construction* , supra, there is no contemporaneity in this case between the alleged disclaimers of responsibility and the negligent misrepresentations. More important than their timing, however, clauses 13 and 14 of the employment agreement are far from being statements, express or implied, that the respondent and its representative are not assuming responsibility for the representations made to the appellant during the hiring interview about the nature and existence of the Multiview project. Although I am not prepared to hold that nothing less than the clearest and most express disclaimer will suffice to negate a duty of care, something more than clauses 13 and 14 is definitely required. These provisions relate to the right and obligations of the parties in the event of the appellant's termination or transfer. They have nothing to do with representations made during pre- or post-contractual negotiations, let alone disclaimers for said representations.

90 Assuming, for the sake of argument, that the principle set out in the judgment of the Court of Appeal is correct in law (i.e., "it is a sufficient disclaimer if the contract contains terms which contradict or are inconsistent with the representations relied upon" (p.183)), there are *no* inconsistencies in the case at bar between clauses 13 and 14 of the contract and the representations *relied on* by the appellant. The only way to find such an inconsistency is to agree with Finlayson J.A. and the respondent that the representations relied on by the appellant amount to a warranty of job security. However, as noted above, the representations in question are *not* of this nature. Rather, they are representations that a particular job would exist and that it would have certain features. As the trial judge found, the representations made during the job interview were firm representations "that the [respondent] company was committed to the development of additional modules of 'Multiview'" (p.397), and there were implicit representations "that there was a reasonable plan in existence for the additional modules and that the company had made a financial commitment in the way of budgetary provisions for such development" (p.398). Characterizing the representations in question as a warranty of job security seems particularly strained because Mr. Johnston actually indicated that the project would last only two years. Thus, Mr. Johnston did not represent that the position would last forever, although he certainly did represent that it would exist.

91 Again, the appellant's claim is not that Mr. Johnston negligently misrepresented the length of time he would be working on Multiview or the conditions under which his employment could be terminated. He does not argue that Cognos, through its representative, breached a duty of care by negligently misrepresenting his security of employment with the respondent company. Rather, the appellant argues that Mr. Johnston misrepresented the nature *and existence*

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of the employment opportunity being offered. It is on these latter representations that the appellant relied in leaving his relatively secure and well paying job in Calgary. The employment agreement neither expressly nor impliedly states that there may be no job of the sort described during the interview after the appellant's arrival in Ottawa. Stipulations that an employee can be dismissed without cause upon proper notice or reassigned to another position are not incompatible with a pre-contractual representation that a particular job would exist, as described, should the employee accept employment.

92 As for the respondent's liability, clauses 13 and 14 of the employment agreement are clearly not, on their face, general limitation or exclusion of liability clauses as these expressions are commonly used. The language adopted by the parties is unambiguous. By stretching the common definition of "limitation of liability clause", one could interpret clauses 13 and 14 as "limiting" the respondent's "liability" in the event of a transfer or termination to what is specifically provided therein. However, even if this interpretation were adopted, the respondent's liability *for pre-contractual negligent misrepresentations* is clearly beyond the scope of these provisions. It is trite law that, in determining whether or not a limitation (or exclusion) of liability clause protects a defendant in a particular situation, the first step is to interpret the clause to see if it applies to the tort or breach of contract complained of. If the clause is wide enough to cover, for example, the defendant's negligence, then it may operate to limit effectively the defendant's liability for the breach of a common law duty of care, subject to any overriding considerations. This is not, however, the situation facing this court.

93 Clauses 13 and 14 of the employment agreement, even if characterized as "limitation of liability" clauses, cannot support an interpretation which would enable them to protect the respondent from the breach of a common law duty of care, let alone the breach of the particular duty invoked by the appellant in his action for negligent misrepresentation. These provisions are no more relevant to the outcome of this case than is clause 15 of the contract, permitting Cognos to terminate the appellant's employment for cause. Thus, contrary to the respondent's submission, the third proposition set out in *Central Trust v. Rafuse* , supra, at p. 206, is of no assistance to this appeal, that is, the appellant is not attempting by his tort claim to "circumvent or escape a contractual exclusion or limitation of liability for the act or omission that would constitute the tort". Simply put, there is nothing in the employment agreement for the appellant to circumvent or to escape.

94 Finally, with respect to the respondent's argument that the appellant "affirmed" his contract by his conduct subsequent to his arrival in Ottawa, I would make two brief comments. First, the whole concept of "affirming" a contract is irrelevant in the case at bar as the appellant is seeking to rely on a tort remedy rather than a contractual one. Second, it seems somewhat harsh to characterize the appellant as having affirmed his contract of employment. The appellant found himself in a very difficult job situation, with increasing marital and health problems to exacerbate the situation. In my view, he acted quite reasonably in attempting to mitigate his losses before finally endinghis employment relationship with Cognos.

F. Conclusion

95 In my view, the appellant has established all the required elements to succeed in his action. The respondent and its representative, Mr. Johnston, owed a duty of care to the appellant during the course of the hiring interview to exercise such reasonable care as the circumstances required to ensure that the representations made were accurate and not misleading. This duty of care is distinct from, and additional to, the duty of common honesty existing between negotiating parties. The trial judge found, as a fact, that misrepresentations — both express and implied — were made to the appellant and that he relied upon them, reasonably I might add, to his eventual detriment. In all the circumstances of this case, I agree with the trial judge that these misrepresentations were made by Mr. Johnston in a negligent manner. While a subsequent contract may, in appropriate cases, affect a *Hedley Byrne* , supra, claim relying on pre-contractual representations, the employment agreement signed by the appellant is irrelevant to this action. In particular, clauses 13 and 14 of the contract are not valid disclaimers of responsibility for the representations made during the interview.

V. Disposition

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96 For the foregoing reasons, I would allow the appeal, set aside the judgment of the Ontario Court of Appeal, and restore the judgment of White J., finding the respondent liable and granting the appellant damages in the amount of $67,224. The appellant should have his costs here and in the courts below.

McLachlin J. **(concurring):**

97 I agree with my colleague Iacobucci J. that this appeal should be allowed, although for reasons which are obvious from my reasons in *BG Checo International Ltd. v. British Columbia Hydro & Power Authority* , S.C.C., Nos. 21939 and 21955 (released concurrently) [reported 75 B.C.L.R. (2d) 145], I do not concur in all aspects of his reasons.

98 The first issue raised by this appeal is the effect of the fact that the parties in this case entered into a contract which contained a specific term governing termination. The Court of Appeal (1990), 74 O.R. (2d) 176 concluded that this precluded the plaintiff's action in tort for negligent misrepresentation as to the employment. Finlayson J.A., for the court, stated (at p. 183):

> the respondent Queen stated that he would not have given up his secure position in Calgary for a move to Ottawa that was without permanence, and yet he signed a contract which provided him with no assurances respecting his place of employment or its tenure. To rely on *Hedley Byrne, the negligent misrepresentation must have amounted to a warranty of job security and yet the contract of employment was surely a disclaimer of just that* . No representations as to job security, whether based on performance or on job availability, could have survived the one-month termination notice "without cause" contained in the contract. [Emphasis added.]

99 My colleague rejects this conclusion on the ground that the contractual duties were different from the common law duty associated with the tort of negligent misrepresentation. The misrepresentation concerned "the nature and existence of the employment opportunity being offered." The contract clauses, by contrast, were concerned with the rights and remedies of the parties relating to termination (p. 29) [para. 44].

100 I agree that the pre-contractual representation was different in scope and effect from the contractual obligation. The matter is not merely one of semantics. It turns on the plaintiff's assessment of the risk involved in leaving his employment and joining Cognos. When a person is deciding to enter a contract with terms governing termination, he or she makes an assessment as to the risk of such termination occurring. A stringent term as to termination may not deter the person from entering into the contract if he or she is satisfied that the risk of termination materializing is low. The representation at issue in this case concerned the risk of termination coming about. The representation was not that Cognos would not have the discretion to terminate or transfer the plaintiff on one month's notice. Rather, by implying that the Multiview project was a reality, that it had the financial support of Cognos, and that it has passed through the feasibility and costing stage, Johnston on behalf of Cognos caused the plaintiff to be misled as to the level of the risk to the plaintiff that Cognos might at some point choose to exercise its termination power under the employment contract. The plaintiff, believing Johnston, concluded that the risk of being transferred or terminated was low.

101 To elaborate, a number of situations can be envisaged in which Cognos might have decided to terminate the plaintiff's employment:

> (i) his employment not working out in the Multiview project, for reasons that did not amount to just cause for dismissal (e.g., say his work was mediocre, but not incompetent);
>
> (ii) unanticipated serious financial difficulties being encountered by Cognos, such that a decision might be made to lay off staff;
>
> (iii) the situation that actually developed, of Cognos' Corporate Management Team deciding, when the Multiview project reached the end of the feasibility and costing stage, not to make a financial commitment to proceeding with the full development of the Multiview line of products;

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(iv) Cognos' Corporate Management Team deciding *after* a financial commitment had been made to scale back or terminate the development of the Multiview line of products.

102 The representation excluded the third reason for dismissal, thereby reducing the risk of termination. As found by the trial judge, the plaintiff relied on that representation in deciding to enter into the contract. It turned out to have been negligently made and false. It follows that the plaintiff is entitled to damages for the loss suffered as a result of that representation.

103 The second issue on the appeal is whether the Court of Appeal was correct in concluding that the trial judge imposed too high a duty of care. Finlayson J.A. correctly stated that the duty on Cognos was "no more than a duty to take care that the representations made were responsible and accurate to the knowledge of Johnston and of his principal, Cognos" (p. 186). However, he went on to conclude "What [Johnston] said was truthful, he believed in it, that was enough" (p. 188). With respect, the second statement cannot be supported. It is not enough that the defendant believed what he said; he must have been non-negligent in having formed and expressed that belief. At the same time, Finlayson J.A. exaggerated the duty of care which the trial judge applied, in stating the trial judge held that Johnston "had to divulge to all of the applicants that he interviewed the precise status of the corporate commitment to the development of the new product so that they could make their own assessment" (p. 187). In fact, the trial judge held only that the defendant had a duty not to hold out to applicants that the project was secure when it knew that funding was not approved and knew or should have known that the final approval was not a rubber stamp process and the secure funding was not a foregone conclusion. I agree with my colleague that this is the appropriate standard and that the duty of care with respect to representations made in a pre-employment situation is the same as that which applies generally. I also agree with my colleague that the argument that the representations are non-actionable by their nature must be rejected.

104 I would allow the appeal on the terms proposed by Iacobucci J.

. . . . .

Appeal allowed.

Footnotes

* Stevenson J. took no part in the judgment.

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TAB 7

2016 ONCA 747
Ontario Court of Appeal

Singh v. Trump

2016 CarswellOnt 16134, 2016 ONCA 747, [2016] O.J. No. 5285, 271 A.C.W.S. (3d) 503, 408 D.L.R. (4th) 235, 62 B.L.R. (5th) 216, 76 R.P.R. (5th) 177

Sarbjit Singh (Plaintiff / Appellant) and Donald John Trump Sr., Trump Toronto Hotel Management Corp., Trump Marks Toronto LP, Talon International Inc., Talon International Development Inc., Val Levitan, Alex Shnaider and Toronto Standard Condominium Corporation No. 2267 (Defendants / Respondents)

Se Na Lee (Plaintiff / Appellant) and Donald John Trump Sr., Trump Toronto Hotel Management Corp., Trump Marks Toronto LP, Talon International Inc., Talon International Development Inc., Val Levitan, Alex Shnaider and Toronto Standard Condominium Corporation No. 2267 (Defendants / Respondents)

Paul Rouleau, K. van Rensburg, M.L. Benotto JJ.A.

Heard: June 23, 2016
Judgment: October 13, 2016
Docket: CA C60787

Proceedings: reversing *Singh v. Trump* (2015), 47 B.L.R. (5th) 269, 2015 CarswellOnt 10437, 2015 ONSC 4461, Perell J. (Ont. S.C.J.)

Counsel: Mitchell Wine, Kevin D. Sherkin for Appellants
Symon Zucker, Melvyn L. Solmon, Nancy J. Tourgis for Respondents

Subject: Civil Practice and Procedure; Contracts; Corporate and Commercial; Property; Securities; Torts

APPEAL by plaintiffs from judgment reported at *Singh v. Trump* (2015), 2015 ONSC 4461, 2015 CarswellOnt 10437, 47 B.L.R. (5th) 269 (Ont. S.C.J.).

***Paul Rouleau J.A.*:**

1 In the mid-2000s, Sarbjit Singh and Se Na Lee each bought a Hotel Unit in the Trump International Hotel, a five-star building to be built in Toronto's financial district. Mr. Singh and Mrs. Lee were both middle-class residents of the Greater Toronto Area and had no intention of occupying the Hotel Units themselves. Instead, they bought the units as investments, expecting that they would profit by participating in the hotel's "Reservation Program".

2 Under the Reservation Program, owners of individual Hotel Units could place their units in a common pool of rooms to be rented out at luxury rates by the hotel's operator. Their expectation was that high occupancy and rental rates at the one-of-a-kind Trump International Hotel would provide healthy returns, even after deducting monthly expenses such as property tax, mortgage payments and housekeeping.

3 Neither Mr. Singh nor Mrs. Lee were sophisticated investors, in real estate or otherwise. Both had to borrow heavily from family to finance their purchases. Both believed that buying into the Trump project would be an excellent investment. And in time, both came to realize that they were wrong.

4 In separate but similar actions, Mr. Singh and Mrs. Lee sued for rescission and damages, claiming they were misled by marketing materials that projected impressive profit margins for purchasers who participated in the Reservation

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Program. They brought motions for partial summary judgment against the respondents Talon International Inc. ("Talon"), Donald John Trump Sr. ("Trump"), Val Levitan and Alex Shnaider. The motions judge dismissed the motions and, in addition, dismissed the claims against Trump, Levitan and Shnaider in their entirety. This is an appeal from that decision.

A. BACKGROUND

5 The motions judge exhaustively reviewed the factual background in his lengthy reasons. I will focus on the details necessary to decide the appeal.

(1) The Trump International Hotel project

6 In the early 2000s, Talon International Development Inc. and its parent Talon launched plans to develop a luxury hotel and condominium in downtown Toronto. At that time, Alex Shnaider was a Director and the Chairman of Talon. Val Levitan was a Director and the Chief Executive Officer and President of Talon. Mr. Levitan had no previous experience in construction, hotel management, or operations.

7 Talon joined forces on the project with Donald J. Trump Sr., the New York-based developer, reality television personality and now presidential candidate. It entered into a licence agreement with Trump Marks Toronto LP to use the Trump name and trademarks for the building, which would be called Trump International Hotel & Tower. Talon also entered into an agreement with Trump Toronto Hotel Management Corp. to operate the Trump International Hotel.

8 The Trump International Hotel & Tower was intended to be, and was ultimately built as, a 70-storey mixed-use complex at the corner of Bay and Adelaide Streets in Toronto's downtown core. The building would contain two condominiums, one composed of residential condominium units and the other composed of full-service luxury hotel guestroom condominium units. Talon proposed to market and sell both types of units to the general public.

9 Persons who bought Hotel Units would have to participate in a maintenance and operation program to cover expenses related to the upkeep of the hotel. Crucially for purposes of these actions, they would also be given the option of participating in the hotel's Reservation Program. Under the Reservation Program, the hotel would rent the purchasers' units out through its own system when the purchasers themselves or their guests were not occupying them. After the hotel deducted the expenses related to the Reservation Program, it would remit the rental income to the Hotel Unit purchasers. The Hotel Unit purchasers would use the profits from the room rentals to offset the carrying costs of the condominiums and to generate income.

(2) The Ontario Securities Commission ruling

10 In 2004, Talon's then-lawyers wrote to the Ontario Securities Commission ("OSC") seeking a ruling under s. 74(1) of the *Securities Act*, R.S.O. 1990, c. S.5, which would exempt the sale of the Hotel Units from the dealer registration and prospectus requirements of ss. 25 and 53 of the Act.

11 Talon's lawyers sought this exemption because, under s. 1(1) of the *Securities Act*, the definition of "security" includes "any investment contract". Without conceding the point, Talon's lawyers explained in its application for the exemption that there was "a risk that a Hotel Unit could be considered an investment contract" for purposes of the Act. If so, without an exemption the units could not be sold or resold by real estate brokers, and any sale or resale would have to comply with the dealer registration and prospectus requirements of the Act.

12 In other words, Talon wanted the Hotel Units to be treated as real estate, not as securities.

13 In their application letter to the OSC, Talon's lawyers correctly explained that the test for what constitutes an "investment contract" — which makes it a "security" — is contextual. Generally, an investment contract is found to exist where:

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(a) a person invests his or her money;

(b) in a common enterprise;

(c) with the expectation of profits;

(d) solely, primarily or significantly attributable to the efforts of others.

See *Securities & Exchange Commission v. W.J. Howey Co.*, 328 U.S. 293 (U.S. Sup. Ct. 1945); *Hawaii Commissioner of Securities v. Hawaii Market Center Inc.*, 485 P.2d 105 (U.S. Hawaii S.C. 1971); *Pacific Coast Coin Exchange of Canada v. Ontario (Securities Commission)* (1977), [1978] 2 S.C.R. 112 (S.C.C.).

14 Talon's lawyers acknowledged that, upon applying these criteria, the Hotel Units "could be considered investment contracts because they must provide accommodation for gain or profit by being part of a Reservation Program". "Notwithstanding this interpretation," the lawyers went on, Talon should be exempt from the registration and prospectus requirements of the Act "because of the way in which the Hotel Units will be structured."

15 In particular, Talon's lawyers represented that the units would "not be marketed or structured as investments for profit or gain". They would be "marketed as luxury hotel condominium units entailing exclusive occupancy rights, coupled with an opportunity to defray related ownership expenses in connection with periods of non-occupancy through voluntary participation in the Reservation Program." Neither Talon nor the sales agents would "make any representation that any Hotel Unit will be able to be rented at any particular rate, or for any particular period of time".

16 Talon's lawyers explained that:

> In keeping with this marketing approach of emphasizing the predominance of the luxury transient hotel occupancy features of Hotel Units, prospective purchasers of Hotel Units will not be provided with rental or cash flow forecasts or guarantees or any other form of financial projection or commitment on the part of [Talon].

17 In a ruling dated May 25, 2004 (the "OSC Ruling"), the OSC granted Talon the exemption it requested. The key passages state:

> UPON the application of Talon International Inc. (the "Applicant") to the Ontario Securities Commission (the "Commission") for a ruling pursuant to s. 74(1) of the Act (the "Application") that the sale by the Applicant of hotel condominium units within a certain building to be known as Trump International Hotel & Tower ... will not be subject to sections 25 and 53 of the Act;
>
> AND UPON considering the Application and the recommendation of the staff of the Commission;
>
> AND UPON the Applicant having represented to the Commission as follows:
>
> .....
>
> > 23. Hotel Units will be marketed primarily as first-class luxury hotel condominium units to be used for short-term transient hotel occupancy or for longer term occupancy. The Reservation Program is merely a secondary feature which offers participating purchasers a means to defray related ownership expenses, as opposed to an investment vehicle for making a gain or profit.
> >
> > 24. Prospective purchasers of Hotel Units will not be provided with rental or cash flow forecasts or guarantees or any other form of financial projection or commitment on the part of the Applicant.
>
> .....

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> 29. The economic value of a luxury hotel condominium of this type will be attributable primarily to its real estate component because Hotel Units will be marketed as luxury transient occupancy hotel condominium properties and will not be offered and sold with an emphasis on the expected economic benefits of the Reservation Program and the Reservation Program Agreement.
>
> [Emphasis added.]

18 The ruling was clear: Talon was not to market the Hotel Units by emphasizing that prospective purchasers could profit through the Reservation Program. The Reservation Program was "merely secondary" to the primary marketing pitch that prospective purchasers could own a luxury Hotel Unit for their personal use. Any participation in the voluntary Reservation Program would simply allow purchasers to "defray" their expenses. And Talon was prohibited from providing prospective purchasers with "forecasts or guarantees or any other form of financial projection or commitment" related to the Reservation Program.

19 The OSC Ruling also required that before entering into an agreement of purchase and sale with a prospective purchaser, Talon would deliver an offering memorandum in the form of a disclosure statement required under the *Condominium Act, 1998*, S.O. 1998, c. 19. This Disclosure Document would include information about "the risk factors that make the offering of Hotel Units a risk or speculation" and explain that prospective purchasers would have a statutory right of action for misrepresentation in the offering memorandum under s. 130.1 of the *Securities Act*. Prospective purchasers would also be informed of their right under the *Condominium Act* to rescind an agreement of purchase and sale within ten days of receiving the Disclosure Document or a material amendment to the Disclosure Document.

(3) Marketing of the Hotel Units and the Estimates

20 Following the OSC Ruling, Talon began marketing the Hotel Units. It set up a sales centre on the building site and put ads in newspapers, magazines and other media. Visitors to the sales centre and to the Trump Tower website could watch a PowerPoint presentation that opened with a smiling Mr. Trump proclaiming: "It's going to be the most elegant building there is. There won't be a building to even compete with it. We're going to do something very special in Toronto."

21 Adina Zak was one of Talon's sales representatives who met with prospective purchasers at the sales centre. She deposed, and the motions judge accepted, that the Hotel Units were sold on the basis of the hotel's location, the fact that it was a turn-key operation, and on the strength of the Trump brand. The pitch was successful: of the 261 available Hotel Units, contracts for sale were entered into for 206 units.

22 Ms. Zak denied that the Hotel Units were marketed as investments but the motions judge rejected that evidence. He found as a fact that the Hotel Units "were sold as an investment with a potential for capital gain and with ongoing income gains that would more than cover expenses." The motions judge explained, at para. 59:

> I do not accept Ms. Zak's evidence that that she never spoke to prospective purchasers about the subject of revenues or mortgages, nor that she did not ever sell the Hotel Units based upon the room rates or occupancy rates. She said she did not discuss with the purchasers the income they might earn or the estimated return on investment, but I do not believe her. These matters were all discussed with potential purchasers.
>
> [Emphasis added.]

23 The plaintiffs Mr. Singh and Mrs. Lee both visited the sales centre and met with Ms. Zak in December 2006 and April 2007, respectively. Mr. Singh had heard about the Trump project from a friend and Mrs. Lee's husband Andrew had seen an ad for it in the newspaper.

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24 The cornerstone of the plaintiffs' claims is a document that Ms. Zak presented to each of them when they met with her to discuss buying a unit in the Trump International Hotel: the "Estimated Return on Investment". I will refer to this document as "the Estimates" in the balance of these reasons.

25 As the motions judge explained, the Trump International Hotel marketing materials, including the PowerPoint presentation, showed four different versions of the Estimates reflecting various expenses and revenues scenarios from four different types of hotel suites. Ms. Zak also prepared customized versions of the Estimates for prospective purchasers who visited the sales centre based on the type of unit they were interested in purchasing.

26 The Estimates contained in the PowerPoint presentation set out different sample units. The units were described in the PowerPoint presentation with the following information:

- the purchase price of the unit, ranging from $784,000 to $843,000;
- monthly common expense fees, ranging from $1,827 to $2,081;
- property taxes, estimated to be at 2% of the purchase price;
- mortgage interest, estimated to be at a 6% interest rate;
- a daily occupancy (housekeeping) fee of $60;
- the average occupancy rate of the hotel, ranging from 55% to 75%;
- the estimated daily room rental rate, ranging from $550 to $600;
- the yearly return earned by an investor in the hotel unit, which, depending on the unit and occupancy rate range from $18,144.41 to $63,627.70;
- a bottom line, bolded annual "return on cash invested", ranging from 6.46% to 21.57%; and
- the percentage amount of the purchase price to be mortgaged.

27 The Estimates had two disclaimers. At the top of the page in capital letters it read: "FOR DISCUSSION PURPOSES ONLY". At the bottom of the page in bold, it read: "*Please note: This is not a guaranteed investment program*".

28 Mr. Singh's Estimate looked like this:

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ESTIMATED RETURN ON INVESTMENT December 12, 2006

FOR DISCUSSION PURPOSES ONLY

Please note: All figures are in Canadian Dollars.

Suite	[illegible]
Suite Type	[illegible]
Purchase Price	$804,000.00
Monthly Common Expense Fee	$1,825.00
Estimated Daily Rental Rate	$550.00
Daily Occupancy Fee (Housekeeping)	$50.00
Amount of Purchase Price to be Financed	75%

Based on an Occupancy Rate of:	75%	65%	55%
Yearly Expenses			
Common Expense Fees	$21,900.00	$21,900.00	$21,900.00
Occupancy Fees (Housekeeping)	$16,425.00	$14,235.00	$12,045.00
Estimated Property Taxes (2% per annum)	$16,080.00	$16,080.00	$16,080.00
Mortgage (6% interest) P + I	$46,621.55	$46,621.55	$46,621.55
Total Expenses	$101,026.55	$98,836.55	$96,646.55
Yearly Revenue			
Revenue from Suite Rental	$150,562.50	$130,487.50	$110,412.50
Summary			
Yearly Return (Revenue - Expenses)	$49,535.95	$31,650.95	$13,765.95
Cash Invested	$201,000.00	$201,000.00	$201,000.00
Return on Cash Invested	24.64%	15.75%	6.85%

Please note: This is not a guaranteed investment program.

Graphic 1

29 When Mr. Singh asked Ms. Zak if the $550 per night room rate was high, she said no because the hotel was a Trump property and would be a five-star hotel. When he asked about the occupancy rates of between 55% and 75%, she replied that since the Trump Hotel would be new and the "buzz" about it would be great, the hotel would be fully occupied.

30 Mrs. Lee's Estimate was similarly promising. Based on a unit which cost $857,000 and would rent out at $600, Mrs. Lee's annual "return on cash invested" ranged from 7.75% at a 55% occupancy rate to 20.90% at a 75% occupancy rate. Her Estimate looked like this:

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ESTIMATED RETURN ON INVESTMENT April 16, 2007

FOR DISCUSSION PURPOSES ONLY

Please note: All figures are in Canadian Dollars.

Suite	[illegible]
Suite Type	[illegible]
Purchase Price	[illegible]
Monthly Common Expense Fee	[illegible]
Estimated Daily Rental Rate	[illegible]
Daily Occupancy Fee (Housekeeping)	[illegible]
Amount of Purchase Price to be Financed	[illegible]

$ 171,400 Total
now $85,700
Oct 07 42,850
April 08 42,850
- name, passport, Social Ins,
- DOB
- contact info

Based on an Occupancy Rate of:	[illegible]	[illegible]	[illegible]
Yearly Expenses			
Common Expense Fees	$24,936.00	$24,936.00	$24,936.00
Occupancy Fees (Housekeeping)	$16,425.00	$14,235.00	$12,045.00
Estimated Property Taxes (2% per annum)	$17,140.00	$17,140.00	$17,140.00
Mortgage (6% interest)	$43,068.88	$43,068.88	$43,068.88
Total Expenses	$101,569.88	$99,379.88	$97,189.88
Yearly Revenue			
Revenue from Suite Rental	$164,250.00	$142,350.00	$120,450.00
Summary			
Yearly Return (Revenue - Expenses)	$62,680.12	$42,970.12	$23,260.12
Cash Invested	$299,950.00	$299,950.00	$299,950.00
Return on Cash Invested	20.90%	14.33%	7.75%

Please note: This is not a guaranteed investment program.

Graphic 2

31 Ms. Zak told the Lees that the unit would carry itself even at the 55% occupancy rate, but that in any event 55% occupancy was a worst-case scenario because of the Trump name.

32 Both Mr. Singh and Mrs. Lee decided to buy.

33 Mr. Singh had been discharged from bankruptcy three years earlier and was earning approximately $55,000 a year as a warehouse supervisor. He did not have enough money for the deposit. His father, a retired welder, agreed to help and took out a line of credit on his own home to finance the loan.

34 Mrs. Lee was a homemaker and her husband worked as a mortgage underwriter. Mrs. Lee's parents loaned her the money for the deposit. Although the Lees' unit was put in Mrs. Lee's name, her husband took the lead throughout the events leading to this litigation.

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35 Mr. Singh deposed that he relied "heavily" on the information Ms. Zak gave him. He agreed in cross-examination that there was no "guarantee" about the occupancy rates reflected in the Estimates, but explained:

> [S]he was telling us that this is what they have estimated, and this is what the month...daily rent would be for the property through whatever channels that they got their information from. So to me, I relied heavily on this, because knowing that her words were, "This is like having an extra income to your home," that you could actually do that.... The way I looked at this is I took the lowest amount, 55 percent. With that yearly return, I said even if it did a lot less than that, I would still even break even to that point.

36 Mrs. Lee also deposed that she relied on the Estimates in deciding to buy a Hotel Unit. She said:

> The Estimate was very important to me in my consideration of a purchase. We could not afford to purchase a unit without any income as we did not even [have] the money for the down payment let alone for the annual carrying costs. The Estimate gave me confidence that our purchase of a Hotel Unit would be a good investment for our children.

37 As it turned out, the Estimates bore no relation to financial reality. The motions judge found as a fact that the Estimates were "deceptive documents" and "replete with misrepresentations of commission, of omission, and of half-truth": at para. 212.

38 Contrary to Mr. Singh's belief that the Estimates were based on "whatever channels that they got their information from", the motions judge found that the figures in the Estimates were merely hypotheticals dreamed up by Talon's principal Mr. Levitan who, it will be recalled, had no previous experience in the hotel business. The motions judge found, at para. 213:

> The Estimates' specifications of hotel rates and occupancy rates, which emanated from Mr. Levitan's mind, were, at best, just opinions or forecasts. However, they were uninformed and ill-informed opinions, and his figures were essentially just pick-a-number speculation about what might be charged and what might happen in the marketplace.

(4) The Disclosure Documents

39 Both Mr. Singh and Mrs. Lee signed agreements of purchase and sale within days of visiting Ms. Zak at the sales office. (Mr. Singh deposed that Ms. Zak had told him that the units were selling very quickly and he had to decide in the next day or so whether to buy.) Talon sent back a fully executed agreement of purchase and sale along with the Disclosure Document required by the OSC Ruling. Both plaintiffs deposed that the Disclosure Document was very thick (it was approximately 300 pages in length) and hard to understand. Neither read the Document in any detail. Mr. Singh handed the Document over to his lawyer.

(5) The closing and the Statement of Adjustments

40 In November 2008, Talon wrote to its purchasers advising that the closing had been extended from March 2009 to November 2010. In August 2010, Talon wrote again, requesting a further extension of the closing from November 2010 to as late as December 2011. Talon later requested three additional extensions of the closing.

41 The motions judge described the choice Talon set out in these letters, at para. 152: "Talon framed the choice for purchasers as whether they wished to take interim occupancy earlier and pay fees but not have any offsetting hotel revenue (since the Trump Hotel was not to open until January 31st, 2012) or to sign the amendment and align interim occupancy with the opening of the hotel."

42 Both Mr. Singh and Mrs. Lee deposed that they agreed to the extensions because they didn't think they had any choice. Both said that if they had known they could withdraw from their agreements of purchase and sale, they would have. They weren't alone: all the purchasers agreed to the extensions.

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43 The Trump International Hotel opened on January 31, 2012. On February 17, 2012, Talon provided purchasers with the interim occupancy closing documents, for a February 24 closing.

44 The closing documents included an Interim Statement of Adjustments setting out the fees purchasers would have to pay during interim occupancy. The figures were markedly different from those set out in the Estimates.

45 Mr. Singh's monthly fee statement totalled $8,306.13, broken down as follows:

Estimated Total Common Expenses:	$2,931.98
Estimated Realty Taxes:	$2,389.75
Interest on Deferred Purchase Monies:	$2,028.83
HST on Occupancy Fee:	*$955.57*
Total	$8,306.13

46 The combined common expense and realty tax numbers shown were $2,156.73 — or 68% — higher than the common expense and realty tax numbers ($1,825 and $1,340, respectively) set out in his original Estimate. Fees of $955.57 for HST, reflected in the Interim Statement of Adjustments, were not even listed in the Estimate originally given to Mr. Singh. Mrs. Lee got a similarly unpleasant surprise: her combined monthly fees for common expenses and realty taxes were $5,291.77, which is $1,785.44 — or 51% — higher than the monthly common expenses and realty taxes described in her original Estimate ($2,078 and $1,428.33, respectively). [1] An amount of $947.89 for HST also appeared for the first time.

47 Talon also sent purchasers a Maintenance Agreement containing expenses that had never been disclosed before: an annual management fee of between 3% to 3.25% of the Hotel Unit revenue; and a furniture, fixtures and equipment fund, which would be 2% of Hotel Unit revenue for 2013, 3% for 2014, and 4% for 2015. The Maintenance Agreement also listed a per use occupancy fee and, although it had been set out in the Estimates, the amount was now higher.

48 Finally, Talon revealed for the first time that Hotel Unit purchasers would have to pay a $48 fee for every night their units were rented out. This information appears in a document called "Reservation Program Frequently Asked Questions" that Talon emailed to purchasers four days before the interim occupancy closing.

49 Mr. Singh and Mrs. Lee signed all the required documents and took interim occupancy.

(6) The interim occupancy period

50 The Reservation Program provided purchasers with quarterly operating statements approximately 30 days after the end of each quarter. During the interim occupancy period, purchasers received statements for the period of February 24 to September 30, 2012.

51 As the motions judge found, all the purchasers lost substantial amounts of money in all three of the start-up quarters. As an illustration, Mr. Singh's losses during the interim occupancy period totalled $29,113.62, an average loss of about $4,000 per month:

Date	Revenue	Occ. %	Avg. Rate	Per Use	Res. Fee	HST	Net Pmt.{*}	Occ. Fee{**}	Gain/Loss
Feb.24-Mar.31	$4,210.00	18.92%	$601.43	$455.00	$336.00	$102.83	$3,863.47	$10,024.64	**-$6,161.17**
Apr.1-June 30	15,875.65	46.15%	377.99	2,795.00	1,968.00	619.19	10,493.46	24,918.39	**-14,424.93**
July 1-Sept.30	11,149.30	26.09%	464.55	1,560.00	1,152.00	352.56	8,084.74	16,612.26	**-8,527.52**

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Total	**$31,234.95**	**33,18%**	**$427.88**	**$4,810.00**	**$3,456.00**	**$1,074.58**	**$22,441.67**	**$51,555.29**	**-$29,113.62**

Notes: * Payment to Owner in Q1 includes one-time HST payment of $547.30** Singh did not pay September Occupancy Fee of $8,306,13

52 As this table shows, the occupancy rates during this period ranged from just under 19% to just over 45% — well below the "worst-case scenario" of 55% that was in Mr. Singh's Estimate. The room rental rates started at a promising $601.43 per night, but then dipped to below $400 per night before rising to $464.55 — again, far lower than the $550 rate listed in Mr. Singh's Estimate. At the same time, the occupancy fees, which included common expenses, realty taxes, interest on deferred purchase monies and HST, were far higher than the amounts listed in the Estimate. The combination of much lower than expected revenue and much higher than expected expenses wiped out any possibility of profit.

53 Mrs. Lee fared even worse. She lost $36,288.16, an average loss of about $5,000 per month:

Pate	Revenue	Occ. %	Avg. Rate	Per Use	Res. Fee	HST	Net Pmt.{*}	Occ. Fee	Gain/Loss
Feb.24-Mar.31	$5,040.00	29.73%	$458.18	$715.00	$528.00	$161.59	$4,290.61	$9,944.02	**-$5,653.41**
Apr.1-June 30	16,806.50	54.95%	336.13	3,250.00	2,400.00	734.50	10,422.00	24,717.99	**-14,295.99**
July1-Sept.30	12,593.00	35.87%	381.61	2,145.00	1,584.00	484.77	8,379.23	24,717.99	**-16,338.76**
Total	**$34,439.50**	**42.73%**	**$366.38**	**$6,110.00**	**$4,512.00**	**$1,380.86**	**$23,091.84**	**$59,380.00**	**-$36,288.16**

(7) Final closing and the complaint to the OSC

54 On October 22, 2012, the Trump Hotel Condominium was registered in the Land Registry Office for the Land Titles Division of Toronto. This created Toronto Standard Condominium Corporation No. 2267. At the end of October 2012, Talon advised the purchasers that final closing would be on November 29, 2012.

55 By that time, the Toronto business press began reporting on the hotel's poor performance. Messrs. Shnaider and Levitan issued a public statement reassuring purchasers and the public that the losses were growing pains and that investors had to expect it would take some time to "ramp up" and "stabilize".

56 In November 2012, a lawyer retained by the plaintiffs wrote to the OSC and asked that it investigate possible breaches of the OSC Ruling. The letter argued that Talon had provided prospective purchasers with prohibited "financial projections" in the form of the Estimates. It also argued that Talon and its agents "made oral representations to prospective purchasers which emphasized the Reservation Program as an investment vehicle. The Reservation Program became the principal feature of the hotel operation and investment."

57 The OSC asked Talon to delay final closing and asked for it to respond to several questions about how the Hotel Units were marketed and sold.

58 In its response, Talon represented that it complied with the OSC Ruling. It stated that while it had not had time to undertake a "comprehensive assessment" of how the Estimates were presented to prospective purchasers, based on the "best recollection" of Talon's management, the information in the Estimates "was presented to purchasers as nothing more than an illustration or example. The illustration was provided to prospective purchasers as simply one component of the materials made available to them."

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59 In any event, Talon submitted that the Estimates did not constitute a rental or cash flow forecast, a guarantee, a financial projection or a commitment of the type prohibited by the OSC Ruling. Instead, the Estimates were "simply illustrative of certain scenarios in respect of a particular Hotel Unit to assist prospective purchasers in making an informed investment decision."

60 On December 4, 2012, the OSC advised that it would not be pursuing regulatory action against Talon. No reasons were provided.

61 On December 14, 2012, the Hotel Units finally closed. Only 50 of the 206 purchasers opted to close on the sale.

62 Mr. Singh was one of the 156 who backed out. His losses as of December 2014 (which included ongoing interest on the loan to his father) totaled $248,064.58. He commenced his action on November 30, 2012. Mrs. Lee was one of the 50 who closed.

63 About ten months after closing, Talon convened a meeting of the owners and advised them that it would take approximately five years for the hotel to become profitable.

64 Mrs. Lee stuck it out and suffered substantial losses in every quarter from December 2012 to March 2015. Her total losses as of December 2014 were $991,576.92. Mrs. Lee commenced her action in February 2015.

B. THE MOTIONS FOR PARTIAL SUMMARY JUDGMENT

65 The plaintiffs' motions for partial summary judgment proceeded only against Talon, Shnaider, Levitan and Trump and were with respect to the alleged breach of the OSC Ruling and the misrepresentation by Talon. There were three lines of attack pursued before the motions judge, all of which focused on the Estimates.

(1) The claim against Shnaider, Levitan and Trump.

66 At the outset of his reasons, the motions judge dismissed the plaintiffs' motions as against Shnaider, Levitan and Trump. The plaintiffs were not attempting to pierce the corporate veil and, in the motions judge's view, there was no conduct on the part of these defendants that was outside of their role in the corporations. Further, the simple fact that Trump's name was associated with the project did not attract personal liability.

67 Despite the absence of a cross-motion for summary judgment, the motions judge considered it appropriate to dismiss the actions in their entirety as against all three individual defendants.

(2) The claim against Talon

(a) First allegation: Talon violated the OSC Ruling

68 The motions judge considered and rejected the defendant's submission that issue estoppel applied against the plaintiffs as a result of the OSC's public statement of December 4, 2012 that it would not be pursuing regulatory action against Talon. In his view, the OSC's review and public statement was not a binding determination as to whether the OSC Ruling had not been breached. Moreover, he held that the plaintiffs should not be bound by a decision made in a proceeding in which they did not have an opportunity to participate. That ruling was not challenged on appeal.

69 The plaintiffs argued that Talon violated the OSC Ruling in two ways. They claimed that the resulting agreements of purchase and sale were illegal contracts and that they were entitled to rescission as a private law remedy.

70 First, the plaintiffs submitted, Talon marketed the Hotel Units as "investment contracts" by emphasizing the Reservation Program as a vehicle for regular profits. This was contrary to paras. 23 and 29 of the OSC Ruling, which mandated that the units would be marketed "primarily" for the purchasers' own use, and that the Reservation Program was "merely secondary" and simply offered a way to "defray" ownership expenses.

71 The motions judge rejected this argument. He held that "Talon marketed the Hotel Units precisely in the way that it undertook to do in its application": at para. 98.

72 He explained, at para. 100: "The Reservation Program was an integral part of the marketing of the Hotel Units, but it did make the selling of Hotel Units, the selling of an investment contract." I pause here to note that the respondents say that this sentence contains a typo and should read: "The Reservation Program was an integral part of the marketing of the Hotel Units, but it did [not] make the selling of Hotel Units, the selling of an investment contract."

73 The motions judge continued, at paras. 100 and 104:

> There is an excruciating subtle point here because the Hotel Units were likely investment contracts. The point, however, is not whether Talon had investment contracts to sell, which is a debatable point, the point being made by the OSC's ruling is that whatever Talon had to sell, it should not sell it as an investment contract.
>
> . . . . .
>
> [I]n the case at bar, it is not necessary to actually determine whether Talon had an investment contract to sell. The point is that whatever it had to sell, it could not and should not be sold as an investment contract. I find as a fact that Talon did not sell whatever it had to sell as an investment contract.

74 The motions judge explained that when the OSC issued its ruling in 2004, it knew that a purchaser was buying a hotel condominium unit and that it was "very likely" the purchaser would participate in the Reservation Program. It also knew that a purchaser would receive financial information and budgets with respect to the operation of the condominium corporation and the hotel. "In other words," the motions judge held, "the OSC knew and anticipated and even directed that purchasers would receive financial information about the operation of the Reservation Program and of the hotel.... [T]he OSC would not have intended to prohibit a manner of sale that was inevitable": at paras. 105-107.

75 Second, the plaintiffs argued that the Estimates breached para. 24 of the OSC Ruling, which prohibited Talon from providing "rental or cash flow forecasts or guarantees or any other form of financial projection or commitment". The parties agreed that the Estimates were not rental guarantees, cash flow guarantees or a type of financial commitment. But the plaintiffs maintained that the Estimates were rental or cash flow forecasts or a form of financial projection. Although Talon agreed that the OSC Ruling prohibited providing prospective purchasers with either forecasts or projections, it argued that the Estimates were not forecasts or projections. They were simply illustrations of how the Reservation Program might function.

76 The motions judge took a different approach. He did not agree that para. 24 of the ruling prevented Talon from providing forecasts or estimates. He interpreted para. 24 "just to exclude financial commitments or guarantees by Talon of the financial returns of the hotel through the Reservations Program." He explained: "Another way to approach the interpretation of the OSC's ruling is that the adjectives are to be read as modifying or describing one type of commitment": at para. 114.

77 The motions judge held, at para. 115: "[O]nce the Plaintiffs conceded that the Estimate was not a guarantee or financial commitment on the part of Talon, which it clearly was not, it lost the debate about whether the OSC's ruling was breached".

(b) Second allegation: misrepresentation in the offering memorandum under s. 130.1 of the Securities Act

78 The plaintiffs argued that the Estimates constituted misrepresentations. As such, they had a statutory cause of action under s. 130.1 of the *Securities Act*, which provides a remedy for purchasers where there is a misrepresentation in an offering memorandum.

79 The motions judge rejected this argument. He held that, because the Estimates "came before and [were] extraneous to" the offering memorandum or Disclosure Documents directed by the OSC, they were outside of the scope of the Act.

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(c) Third allegation: misrepresentation in the Estimates

80 Finally, the plaintiffs claimed that Talon, Shnaider, Levitan and Trump were liable for the misrepresentations contained in the Estimates. Although the plaintiffs argued the misrepresentations could be viewed as fraudulent in nature, the motions judge determined that the fraudulent misrepresentation claim had not been pleaded. As a result, he made no findings and said little in respect to that ground. He then turned to the claim for negligent misrepresentation and agreed that two misrepresentations had been made out:

> 1. Talon misrepresented that the Estimates were done based on the best available information to Talon to forecast potential revenue, expenses and net income, when in truth, the Estimates overstated revenue and understated expenses; and
>
> 2. Talon misrepresented that the Hotel Units would be profitable immediately when the Trump Hotel opened for business.

81 The motions judge was satisfied the plaintiffs had established four out of the five elements required to prove a claim of negligent misrepresentation, as set out in *Queen v. Cognos Inc.*, [1993] 1 S.C.R. 87 (S.C.C.): (1) the defendants owed them a duty of care; (2) the defendants made an untrue, inaccurate or misleading representation; (3) the defendants did so negligently; and (4) the plaintiffs suffered damage as a result. It was in this context that the motions judge described the Estimates as "deceptive documents" that were "replete with misrepresentations of commission, of omission, and of half-truth". He explained, at para. 215: "Mr. Levitan had no training, experience, or justification from actual research to make any projections about the revenue streams for the new hotel in Toronto. What actually happened shows how inaccurate Mr. Levitan's guesswork was."

82 Despite these strong words, the motions judge held that the plaintiffs failed to establish the fifth required element: that they *reasonably* relied on the misrepresentation.

83 The motions judge accepted the plaintiffs' evidence that they had relied on the Estimates in making their decision to buy the Hotel Units. He went on to explain, however, that while the plaintiffs would not have known that the Estimates constituted misrepresentations:

> ... nevertheless, they would and should have known that it would be unreasonable for a prospective purchaser to rely on the Estimates or to be induced by the Estimates to enter into their Agreements of Purchase and Sale. Although Mr. Singh and Mrs. Lee may have subjectively relied on the Estimates in deciding to purchase the Hotel Units, their subjective reliance was objectively unreasonable.

84 The motions judge noted that the Estimates were "for discussion purposes" and were not "a guaranteed investment program". Mr. Singh and Mrs. Lee knew that all investments are risky and those risks were pointed out to them repeatedly in the Disclosure Documents. They knew they had a statutory cooling-off period under the *Condominium Act*, and they had an opportunity to conduct their own due diligence.

85 Further, the motions judge explained that around the time of the interim closings, the plaintiffs came to learn that the Estimates contained "misrepresentations of commission, omission and half-truths" about the quantum of expenses they would be liable to pay. Although the plaintiffs would not have known at that point about the misrepresentations regarding rental and occupancy rates, the motions judge considered that their going ahead with the interim closings "suggests that they were never reasonably relying on the Estimates as the inducement to enter into the Agreements": at para. 229. Rather, they were relying on "their rights and remedies associated with the documents required to be disclosed under the ruling of the OSC and pursuant to the provisions of the *Condominium Act*, 1998."

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86 The motions judge went on to hold that, in any event, the plaintiffs' negligent misrepresentation claim was defeated by the "entire agreement clause and the other exculpatory provisions of the Agreement of Purchase and Sale and the related contracts": at para. 235.

87 The entire agreement clause in the agreement of purchase and sale reads as follows:

> 31. The Vendor and the Purchaser agree that there is no representation, warranty, collateral agreement or condition affecting this Agreement or the Property or supported hereby other than as expressed herein in writing.

88 The Disclosure Document contained various exculpatory statements such as:

> Purchasers are advised that no representations are made with respect to expected or projected rental income. There is no assurance that Hotel Units will be able to be rented at any particular rate or for any particular period of time and the rates and the total income from each Hotel Unit will be affected by, among other things, competitions from other luxury hotels, guest preferences, economic conditions...

89 The Reservation Program agreement contained similar exculpatory statements as well as an entire agreement clause providing that the agreement "supersedes and replaces all prior negotiations and/or agreements made between the parties hereto, whether oral or written, and contains the entire understanding between the parties with respect to the subject matter hereof."

90 The motions judge held, without further analysis, that "there is no unconscionability or public policy reason to justify not enforcing" the clause: at para. 239.

91 Finally, although it was not pleaded, the motions judge dismissed Mrs. Lee's claim as time-barred. He held that she ought to have known about the misrepresentation claims around the time of interim closing in 2012, but she did not commence her action until 2015, which was beyond the statutory two-year limitation period: at para. 242.

C. DISCUSSION

(1) Overview

92 The plaintiffs appeal the motions judge's decision to dismiss the motions as against Talon on all three grounds they raised in the court below. They also appeal the dismissal of the claims against Shnaider, Levitan and Trump.

93 In my view, the appeal as against Talon can be decided on the basis that the motions judge, having found that four of the five elements for a claim of negligent misrepresentation were made out, erred in holding that the plaintiffs failed to establish the fifth element, reasonable reliance.

94 I would also hold that the motions judge erred in enforcing the entire agreement and other exculpatory clauses to bar the plaintiffs' actions. In light of the circumstances and context in which the clauses were entered into, it would be unconscionable to enforce those clauses to bar the plaintiffs' claims.

95 In addition, I would set aside the motions judge's dismissal of Mrs. Lee's claim as time-barred. Although they raised limitation provisions in the *Securities Act* and the *Condominium Act* in their statement of defence, the defendants did not plead the *Limitations Act*, 2002, S.O. 2002, c. 24, Sched. B., nor did they seek leave to amend to do so. Further, they failed to raise a *Limitations Act* defence in their written submissions on the motions for summary judgment. In these circumstances, it was not appropriate for the motions judge to invoke the *Limitations Act* to dismiss Mrs. Lee's claim.

96 I also disagree with the motions judge's conclusion that fraudulent misrepresentation had not been pleaded. Although the statement of claim does not use the words "fraudulent misrepresentation", all of the elements and materials facts for such a claim are pleaded and the claim was brought to the respondents' attention in the factum filed on the

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summary judgment motions. Because the motions judge did not make the necessary factual findings, this claim should simply be remitted to be determined on a subsequent motion or at trial.

97 With respect to the action against Shnaider, Levitan and Trump, I agree that the claims that were the subject of the motions for summary judgment were properly dismissed. In my view, however, the motions judge erred in dismissing the claims against the three individual defendants that were not properly before him.

98 I will elaborate on each point below.

(2) Reasonable reliance

99 As the motions judge indicated, the five elements of a claim for negligent misrepresentation are: (1) a duty of care based on a "special relationship"; (2) a misleading representation; (3) negligence in making the misrepresentation; (4) reasonable reliance on the representation; and (5) damage caused by the reliance: *Queen v. Cognos Inc.*, at p. 110. Only the "reasonable reliance" factor is at issue here.

100 Whether a plaintiff reasonably relied on a defendant's misrepresentations is a question of fact: *NBD Bank, Canada v. Dofasco Inc.* (1999), 46 O.R. (3d) 514 (Ont. C.A.), at para. 81, leave to appeal refused, (1999), [2000] S.C.C.A. No. 96 (Ont. C.A.).

101 As I have just explained, the motions judge accepted that Mr. Singh and Mrs. Lee "subjectively relied" on the Estimates, but held that "their subjective reliance was objectively unreasonable" because:

1. The Estimates were "for discussion purposes only" and "not a guaranteed investment program". The plaintiffs were given various warnings, protections and rights, and as a result, it would not have been objectively reasonable for them to rely on the Estimates for what they knew was a "risky financial investment"; and

2. Once the plaintiffs learned of higher than expected expenses at the time of interim closing, they did not try to back out of their agreements of purchase and sale.

102 On the first point, the fact that the Estimates were "for discussion purposes only" and "not a guaranteed investment program" does not inevitably lead to the conclusion that it would be unreasonable for the plaintiffs to rely upon them. Earlier in his reasons, the motions judge rejected Ms. Zak's evidence that she did not sell the Hotel Units based on room rates and occupancy rates — the very information set out in the Estimates. Instead, he found as a fact that "the Hotel Units were sold as an investment with a potential for capital gain and with ongoing income gains that would more than cover expenses": at para. 59. This information came directly from the Estimates.

103 The motions judge does not explain how his finding that Talon sold the Hotel Units as investments based on the information contained in the Estimates can be reconciled with his finding that the plaintiffs' reliance on those Estimates was unreasonable. In other words, if the basis of the sale was the unit's value as an investment as expressed in the Estimates, why was reliance on that information unreasonable?

104 Further, although I agree with the motions judge's finding that the plaintiffs were warned about the risks of their investment, it does not follow that it was unreasonable for the plaintiffs to rely on the Estimates. The risks acknowledged and accepted were the risks that market conditions could change, that rental rates and occupancy rates could fluctuate, and that their expenses might go up. Those are known, expected risks and the disclaimers in the documentation clearly disclose their existence. It would have been unreasonable for the plaintiffs to rely on representations that these risks did not exist.

105 The actionable misrepresentations, however, were not that risks such as market conditions and fluctuations in rental and occupancy rates did not exist. The misrepresentations were: (1) that the figures in the Estimates were based on the best available information; and (2) that the hotel would be immediately profitable. On the motions judge's own findings, both misrepresentations were established. He found that the figures in the Estimates were based not on hard

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numbers but on Mr. Levitan's "uninformed and ill-informed opinions". Many known expenses were not disclosed or were grossly understated. Moreover, he found that when both Mr. Singh and Mr. Lee pressed Ms. Zak about the high occupancy and rental rates in the Estimates, she assured them that the hotel would be fully booked because it was new and would attract "buzz".

106 I agree with the motions judge that it would have been unreasonable for the plaintiffs to rely on a representation that the Estimates were a guarantee that their investments would pan out exactly as they had hoped. They knew or ought to have known that the Estimates were not a guarantee that the investment would be profitable. They assumed the risk that room and occupancy rates would fluctuate and that they might earn less profit than they originally anticipated. It is unreasonable, however, to conclude that the plaintiffs assumed the risk that the Estimates upon which they decided to invest were simply made up in the first place and that known expenses were either not disclosed or were grossly understated.

107 On the second point, the fact that the plaintiffs learned in 2012 that their expenses would be higher does nothing to undermine the reasonableness of their reliance on the Estimates in 2006 and 2007. Ms. Zak sold the units as an investment using estimates that understated expenses and overstated revenue. She told prospective purchasers that the 55% occupancy rate set out in the Estimates was a worst-case scenario, and that even at that rate the hotel would be profitable. Even after it was revealed to purchasers for the first time at interim closing that expenses had been understated, the plaintiffs had yet to discover that revenue was overstated. Specifically, the room rental rates and occupancy rates set out in the Estimates were unrealistically high and were based on uninformed and ill-informed opinions. As Mr. Singh testified, he was nervous after hearing of the high occupancy fees but he thought he had no choice. He took comfort from the Estimate that indicated that his annual revenue would be more than enough to offset the fees.

108 The motions judge's conclusion that the plaintiffs' reliance on the Estimates was objectively unreasonable is clearly in error and cannot stand. The plaintiffs' reliance on the Estimates was objectively reasonable.

(3) The entire agreement and other exclusionary clauses

109 As noted earlier, the agreement of purchase and sale, the Disclosure Document and the Reservation Program agreement contained various entire agreement and exclusionary provisions. Those clauses, examples of which I have quoted earlier, advised purchasers that they should only rely on the agreements expressed in writing, that no representations were being made as to the projected income from the rental of the Hotel Units and that there were risks that income would not be as projected.

110 Unless inapplicable, unenforceable, or otherwise invalid, contractual provisions such as entire agreement clauses may limit a party's right to sue in tort: *BG Checo International Ltd. v. British Columbia Hydro & Power Authority*, [1993] 1 S.C.R. 12 (S.C.C.), at p. 30. That is because duties based in tort "must yield to the parties' superior right to arrange their rights and duties in a different way": *BG Checo*, at p. 27.

111 In *Tercon Contractors Ltd. v. British Columbia (Minister of Transportation & Highways)*, 2010 SCC 4, [2010] 1 S.C.R. 69 (S.C.C.), Binnie J. (dissenting but supported by a unanimous court on this point) set out the following analytic approach to be used in deciding whether to enforce such clauses, at paras. 122-23:

> The first issue, of course, is whether as a matter of interpretation the exclusion clause even *applies* to the circumstances established in evidence. This will depend on the Court's assessment of the intention of the parties as expressed in the contract. If the exclusion clause does not apply, there is obviously no need to proceed further with this analysis. If the exclusion clause applies, the second issue is whether the exclusion clause was unconscionable at the time the contract was made, "as might arise from situations of unequal bargaining power between the parties" (*Hunter*, at p. 462). This second issue has to do with contract formation, not breach.
>
> If the exclusion clause is held to be valid and applicable, the Court may undertake a third enquiry, namely whether the Court should nevertheless refuse to enforce the valid exclusion clause because of the existence of an overriding

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> public policy, proof of which lies on the party seeking to avoid enforcement of the clause, that outweighs the very strong public interest in the enforcement of contracts.

112 In his reasons the motions judge referenced *Tercon* and the analytical approach described therein. His analysis and application to the facts of this case, however, are contained in their entirety in para. 239 of his reasons:

> [T]he entire agreement and other exculpatory provisions included in the Disclosure Documents or Statements apply and stands in the way of the success of the Plaintiffs' misrepresentation claims. As a matter of interpretation the clauses apply, and there is no unconscionability or public policy reason to justify not enforcing the exculpatory provisions.

113 In my view, the motions judge erred in concluding, without analysis, that it was not unconscionable to enforce the exculpatory provisions. Unconscionability provides that despite the general principle that parties should be held to the bargains that they have made, there are some parties that must be protected and some bargains that should not be enforced: see A. Swan and J. Adamski, *Canadian Contract Law*, 3d ed. (Markham, Ont.: Lexis Nexis, 2012) at para. 9.99.

114 In *Domtar Inc. c. ABB Inc.*, 2007 SCC 50, [2007] 3 S.C.R. 461 (S.C.C.), at para. 82, LeBel and Deschamps JJ. described the doctrine of unconscionability in the context of limitation clauses, a type of clause similar in nature to exclusion or entire agreement clauses:

> Under the doctrine of unconscionability, a limitation of liability clause will be unenforceable where one party to the contract has abused its negotiating power to take undue advantage of the other. This doctrine is generally applied in the context of a consumer contract or contract of adhesion.

115 In *Zippy Print Enterprises Ltd. v. Pawliuk* (1994), 100 B.C.L.R. (2d) 55 (B.C. C.A.), the British Columbia Court of Appeal declined to enforce an entire agreement clause to preclude a claim based on a misrepresentation made to a franchisee. The franchisor had made misleading statements about estimated gross sales, expenses, and profits to induce the franchisee to enter an agreement. In rejecting the enforcement of these clauses, Lambert J.A. expressed the following view, at para. 45:

> A general exclusion clause will not override a specific representation on a point of substance which was intended to induce the making of the agreement unless the intended effect of the exclusion clause can be shown to have been brought home to the party to whom the representation was made by being specifically drawn to the attention of that party, or by being specifically acknowledged by that party, or in some other way.

116 In the present case, the entire agreement clause functioned as a trap to these unsurprisingly unwary purchasers. Neither the Singhs nor the Lees had anything more than minimal investing experience. Their real estate experience was limited to the purchase of their family homes, although Mr. Lee worked as a mortgage agent (as did Ms. Singh beginning in 2008). They would have known little or nothing regarding luxury hotel rental rates and occupancy. And both the Singhs and the Lees signed the agreements of purchase and sale without consulting with a lawyer.

117 The entire agreement clause was well hidden within the agreement of purchase and sale. The agreement of purchase and sale is almost 17 pages long including schedules, with 49 articles that often include sub-clauses of their own. The entire agreement clause is found on page seven, the third of twelve articles under the heading 'General'. Nothing distinguishes this article from the other rectangles of dense black ink nearby. Ms. Zak, the sales representative for both the Singhs and the Lees, acknowledged in her evidence that she never reviewed the entire agreement clause with the plaintiffs.

118 The relevant portion of the entire agreement clause simply states: "The Vendor and the Purchaser agree that there is no representation ... affecting this Agreement or the Property or supported hereby other than as expressed herein in writing." Such a clause would mean nothing to the Singhs or Lees. They gave evidence accordingly. They could not have reasonably been expected to have understood that this meant that the respondents were exempting themselves from any liability flowing from their misrepresentations that induced the Singhs and Lees to sign the contract in the first place.

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119 The Disclosure Document stands on even more unstable ground. Notably, it was not provided to either the Singhs or the Lees until *after* they had signed the agreements of purchase and sale.

120 Even if the exculpatory provisions in the Disclosure Documents should be considered, many of the same factors supporting a finding of unconscionability apply. Although bolded in all-caps, the main exculpatory provision was found about ten pages into a roughly 300-page document. Other than the capitalization and bolding, nothing was done to draw the Singhs' or Lees' attention to the significance of such a clause.

121 Moreover, such a disclaimer comes too late to be of any assistance to the purchaser who has already been induced to enter into an agreement. As Professor McCamus explains with respect to such subsequent disclaimers, "[t]he trap has already been set and triggered. If the contract contains a disclaimer clause, it is simply a better trap": John D. McCamus, *The Law of Contracts*, 2nd ed. (Toronto: Irwin Law, 2012), at p. 365.

122 It would be grossly unfair to enforce these clauses to deny Talon's tort duty not to make negligent misrepresentations to the plaintiffs.

123 Although the above considerations should be sufficient to found a decision declining enforcement of those clauses, further support can be found when the context of the contract formation is considered. As I will explain, I would find that Talon breached and evaded the protections of *Securities Act* by both the marketing of the Hotel Units as investment contracts with emphasis on the Reservation Program as a vehicle for regular profits and the providing of rental and cash flow forecasts or projections that were contrary to the OSC Ruling.

124 In my view, the motions judge erred in concluding otherwise.

125 With respect to the marketing of the Hotel Units, it is to be recalled that Talon's lawyers represented that the Units would "not be marketed or structured as investments for profit or gain" but would rather be marketed "as luxury hotel condominium units entailing exclusive occupancy rights, coupled with an opportunity to defray related ownership expenses in connection with periods of non-occupancy through voluntary participation in the Reservation Program". The motions judge found that Talon marketed the Hotel Units "precisely in the way that it undertook to do in its application" to the OSC (at para. 98) and that "Talon did not sell whatever it had to sell as an investment contract" (at para. 104). He does not explain how this is to be reconciled with his earlier findings. Those findings were that "the Hotel Units were sold as an investment with a potential for capital gain and with ongoing income that would more than cover expenses", and that Ms. Zak "discuss[ed] with the purchasers the income they might earn or the estimated return on investment": at para. 59.

126 Similarly, the motions judge's description of the Reservation Program as "an integral part of the marketing of the Hotel Units" appears on its face to acknowledge that Talon breached the OSC Ruling, which provided in para. 23 that the Reservation Program would be marketed as "merely a secondary feature" to defray ownership expenses, as opposed to an investment vehicle.

127 With respect to the Estimates, the motions judge found that providing financial projections and rental or cash flow forecasts to prospective purchasers of Hotel Units did not contravene the OSC's prohibition against providing "rental or cash flow forecasts or guarantees or any other form of financial projection or commitment". In my view the motions judge's interpretation is simply unreasonable and cannot stand (*L. (H.) v. Canada (Attorney General)*, 2005 SCC 25, [2005] 1 S.C.R. 401 (S.C.C.), at paras. 55-56, 110). The reasonable reading of this provision is that it prevents both the giving of guarantees and commitments and the giving of financial projections and rental or cash flow forecasts. The motions judge's reading of the provision effectively reads out key terms and renders their inclusion meaningless.

128 As to the motions judge's suggestion that the Estimates do no more than give effect to the OSC's implicit assumption that Talon would explain how the Reservation Program functioned, it is apparent from even a cursory review of the Estimates provided to the plaintiffs that they went well beyond such a purpose. The carrying costs of the units as set

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out in the Estimates have nothing to do with the operation of the Reservation Program. The title "estimated return on investment", the layout of the document and the setting out of annualized rates of return on cash invested all show the document to be much more than what the motions judge characterized as "information about the operation of the Reservation Program and of the hotel".

129 In my view, it would be unconscionable and would shock the conscience to allow a party to use an entire agreement or other exculpatory clause to escape liability for misrepresentations made in breach of the OSC's terms for granting an exemption from the *Securities Act* requirements. The entire agreement and other exculpatory clauses would operate to negate a negligent misrepresentation claim and the misrepresentation itself was only possible in this case because Talon evaded protective requirements under the *Securities Act* by obtaining the exemption and then breaching that exemption.

(4) The limitations issue

130 The motions judge found that Mrs. Lee's negligent misrepresentation claim was barred by the *Limitations Act*. He did so despite the fact that the defendants had not pled the *Limitations Act* and had not sought to amend their pleading to include such a plea. Although they raised the issue in oral submissions, the defendants had not raised it in the factum filed on the summary judgment motions.

131 In his reasons the motions judge neither refers to the fact that it was not pleaded nor does he explain why, in the absence of such a plea, he should nonetheless invoke the Act.

132 This court has consistently held that "[t]he expiry of a limitation period is a defence to an action that must be pleaded in a statement of defence": *Collins v. Cortez*, 2014 ONCA 685, [2014] O.J. No. 4753 (Ont. C.A.), at para. 10, per van Rensburg J.A. (citing *S. (W.E.) v. P. (M.M.)* (2000), 50 O.R. (3d) 70 (Ont. C.A.), at paras. 37-38, leave to appeal to S.C.C. refused, (2001), 149 O.A.C. 397 (note) (S.C.C.)). This requirement is embodied in rule 25.07(4) of the *Rules of Civil Procedure*, which Ontario courts have consistently held "applies to pleadings relating to limitations that might bar an action": *S. (W.E.) v. P. (M.M.)* at para. 37. Rule 25.07(4) provides as follows:

> In a defence, a party shall plead any matter on which the party intends to rely to defeat the claim of the opposite party and which, if not specifically pleaded, might take the opposite party by surprise or raise an issue that has not been raised in the opposite party's pleading.

133 Justice Cronk explained the rationale behind the requirement that a party specifically plead a limitation period defence in *Hav-A-Kar Leasing Ltd. v. Vekselshtein*, 2012 ONCA 826, 225 A.C.W.S. (3d) 237 (Ont. C.A.), at para. 69:

> The failure to raise substantive responses to a plaintiff's claims until trial or, worse, until the close of trial, is contrary to the spirit and requirements of the Rules of Civil Procedure and the goal of fair contest that underlies those Rules. Such a failure also undermines the important principle that the parties to a civil lawsuit are entitled to have their differences resolved on the basis of the issues joined in the pleadings.

134 In *S. (W.E.) v. P. (M.M.)*, MacPherson J.A. confirmed that Ontario courts "have consistently held that rule 25.07(4) applies to pleadings relating to limitations that might bar an action": at para. 37. He went on to explain that even though in that case the trial judge had given counsel time to prepare submissions on the issue after he raised it during closing arguments, it did not remove the potential prejudice to P:

> If S had raised the issue in his pleadings, P might have tried to settle, or even have abandoned, her counterclaim. Either decision might have had costs consequences. Another potential source of prejudice arises from the fact that counsel for P might have adopted different tactics at trial. In particular, counsel might have called different or additional evidence to support an argument that the discoverability principle applied (at para. 38).

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135 MacPherson J.A. also noted that at no time during trial, including during closing arguments when the trial judge raised the limitation issue, did S seek to amend his pleadings. Nor did he seek such an amendment during the appeal hearing.

136 In my view, the defendants' failure, in this case, to plead a *Limitations Act* defence or even to seek an amendment to their pleading to do so is, as it was in *S. (W.E.) v. P. (M.M.)*, fatal.

(5) The fraudulent misrepresentation pleading

137 The motions judge stated at para. 201 that "because the fraudulent misrepresentation claim was not pleaded I shall say little about it." The reasons, however, contain no analysis of the statements of claim nor an explanation of how he reached this conclusion.

138 While the factum filed by the plaintiffs on the summary judgment motions focused principally on negligent misrepresentation, it did refer to fraud. For example, the factum stated as follows at para. 351:

> If this Court determines (particularly in the case of Levitan) that the misrepresentation can be characterized as fraudulent then the individual liability of the employee is easier to establish since his actions take on the character of an individual and separate tort. [Footnote omitted.]

139 In response, the defendants' summary judgment factum acknowledged that the plaintiffs claimed Levitan's actions met the test for fraudulent misrepresentation, but then simply stated that the plaintiffs did not specifically plead fraudulent misrepresentation. No specific deficiency in the pleadings was identified, nor was any prejudice claimed.

140 On appeal the respondents again maintain that the pleadings were deficient and, specifically, they argue that the appellants' pleadings do not assert that the defendants knew that the statements were false or were indifferent to their truth or falsity. They further argue that there was no pleading that there was an intention that the appellants would act on the false representations.

141 Although it is not clear from the case law that an intention that the false representation be acted on is a necessary element of a fraudulent misrepresentation claim (see *Combined Air Mechanical Services Inc. v. Flesch*, 2014 SCC 8, [2014] 1 S.C.R. 126 (S.C.C.), at para. 21, and *Bhasin v. Hrynew*, 2014 SCC 71, [2014] 3 S.C.R. 494 (S.C.C.), at para. 88), the pleadings of both Mrs. Lee and Mr. Singh assert that the defendants knew the statements were false (Mrs. Lee's statement of claim at para. 76; Mr. Singh's at paras. 114-116) and that there was an intention that they would be acted upon (Mrs. Lee's statement of claim paras. 97-98; Mr. Singh's at para. 112).

142 The pleadings could certainly have been clearer and the absence of a specific statement that a fraudulent misrepresentation claim was being advanced is of concern. This having been said, the respondents do not argue that they have been taken by surprise or prejudiced. Provided that the particulars and material facts relied upon for a fraudulent misrepresentation claim are pleaded it is not essential that the word "fraud" or "fraudulent" be used: see *Shoppers Drug Mart Inc. v. 6470360 Canada Inc.*, 2014 ONCA 85, 372 D.L.R. (4th) 90 (Ont. C.A.), at para. 54.

143 As a result, I would set aside the motions judge's dismissal of the fraudulent misrepresentation claim. In setting aside the dismissal I should not be taken as finding that the claim has merit. I am simply not prepared to rule on the merits of the claim. Contrary to the appellants' contention, I do not consider the motions judge's findings, such as the finding at para. 213 that some of the information contained in the Estimates "emanated from Mr. Levitan's mind", to be dispositive. While the motions judge was clearly unimpressed with Mr. Levitan's process for coming up with the projections, he never concluded that the misrepresentations were made with knowledge of their falsity or with recklessness as to whether they were true.

144 As a result, because necessary factual findings regarding this claim were not made, I would remit the issue to be decided on a further motion for summary judgment or at trial. In light of the disposition of the appeal, the appellants may

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well decide not to proceed with the fraudulent misrepresentation claim. Should the appellants choose to proceed with that claim, however, and should they succeed in proving fraudulent misrepresentation, different or additional remedies may be available to them.

(6) The dismissal of the actions against Shnaider, Levitan and Trump

145 The appellants argue that the motions judge erred in dismissing the actions against Shnaider, Levitan and Trump. They contend that, although it was open to the motions judge to dismiss those claims that were the subject of the summary judgment motions, it was unfair for him to have dismissed the causes of action pled but not encompassed in the motions before him.

146 I agree.

147 The motions judge correctly noted that on a motion for summary judgment the judge may grant judgment in favour of a responding party, even in the absence of a cross-motion for such relief: *Meridian Credit Union Ltd. v. Baig*, 2016 ONCA 150, 394 D.L.R. (4th) 601 (Ont. C.A.), at para. 17; *King Lofts Toronto I Ltd. v. Emmons*, 2014 ONCA 215, 40 R.P.R. (5th) 26 (Ont. C.A.), at paras. 14-16; *Kassburg v. Sun Life Assurance Co. of Canada*, 2014 ONCA 922, 124 O.R. (3d) 171 (Ont. C.A.), at paras. 50-52.

148 However, a motion judge may not grant or dismiss a claim on a motion for summary judgment that is not within the scope of the motion before him or her. Doing so would deny procedural fairness and natural justice.

149 A fair hearing requires that a party have notice of the matters that will be at issue at the hearing and of how that party may be affected by the hearing's outcome: see *Québec (Commission des relations ouvrières) v. Alliance des professeurs catholiques de Montréal*, [1953] 2 S.C.R. 140 (S.C.C.).

150 In the present case, the grounds set out in the notices of motion are that the plaintiffs were seeking "damages from Talon and the other Defendants for breaches set out in [the] Statement of Claim and *mov[ing] for summary judgment on the basis of the following claims*" (emphasis added). The claims that follow in the notices of motion are those concerning the OSC Ruling and misrepresentations by Talon. They did not include any of the plaintiffs' other claims, such as those based on oppression, collusion, or breach of fiduciary duties.

151 The parties' summary judgment factums were consistent with motions for partial summary judgment limited to the OSC Ruling claims and claims of misrepresentation. The plaintiffs' factum stated that "[t]he legal issues to be determined are as follows: a) Did Talon breach the terms of the Ruling and, if so, what remedy is available to the Plaintiffs; and b) Did these Defendants make any actionable misrepresentations and, if so, what remedy is available to the Plaintiffs."

152 The defendants' summary judgment factum suggested that they understood the limited scope of the motions for summary judgment. Their law and argument section addressed two categories of claims: those arising out of the OSC Ruling and the misrepresentation claims. The response of Trump, Levitan, and Shnaider was limited to arguing that no misrepresentations were made or that, in any event, they were not misrepresentations that would attract personal liability.

153 In their factum the respondents submitted that, if they were successful on the OSC or misrepresentation claims, *those* causes of action should be dismissed. Their requested order was for "the Motion for Summary Judgment [to] be dismissed, and *that the causes of action based upon the breach of the OSC Ruling and misrepresentation be dismissed*, with costs" (emphasis added).

154 For these reasons, I would set aside the motions judge's dismissal of the causes of action against Shnaider, Levitan and Trump that fall outside the scope of the motions for partial summary judgment.

(7) Remedy

155 The appellants argue that the appropriate remedy is to order rescission or, in the alternative, damages.

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156 I agree that Mr. Singh, as a party to an executory agreement that never closed, is entitled to rescission. This court has long held that "[r]escission is available in the case of an executory contract where a material misrepresentation that was an inducement to enter into the contract is established": *Panzer v. Zeifman* (1978), 20 O.R. (2d) 502 (Ont. C.A.). Elaborating on this point, the motions judge correctly stated that rescission may be obtained on the basis of a non-fraudulent misrepresentation where the defendant has made a false statement that was material and that induced the plaintiff to enter the contract, and where the innocent party has sought rescission before the closing of the transaction. Having determined that the elements of negligent misrepresentation are made out, and that these misrepresentations were material and induced Mr. Singh to enter the agreement of purchase and sale that he refused to close in 2012, I find that Mr. Singh is entitled to rescission.

157 The same, however, cannot be said for Mrs. Lee who completed the purchase of the unit. Absent a finding of fraud, in the context of real estate transactions induced by misrepresentation, execution of the agreement has typically been held to constitute a barrier to rescission: *Nesbitt v. Redican* (1923), [1924] S.C.R. 135 (S.C.C.); *Shortt v. MacLennan* (1958), [1959] S.C.R. 3 (S.C.C.); *Kingu v. Walmar Ventures Ltd.* (1986), 10 B.C.L.R. (2d) 15 (B.C. C.A.). The appellants have referred the court to more recent judicial support for the view that execution is a relevant but not decisive factor in determining whether rescission is available, at least in some limited contexts: *S-244 Holdings Ltd. v. Seymour Building Systems Ltd.*, [1994] B.C.J. No. 598 (B.C. C.A.); see also McCamus, at pp. 354-355, and S.M. Waddams, *The Law of Contracts*, 6th ed. (Toronto: Canada Law Book, 2010), at para. 424.

158 Even assuming without deciding that rescission could be a remedy available to Mrs. Lee after having executed her transaction, I would nevertheless not grant rescission in the circumstances of this case. It is not apparent from the record what effect rescission would have on innocent third parties such as Mrs. Lee's mortgagor, who was not made a party to these proceedings. Further, the claim was issued more than two years after she closed the transaction. In these circumstances I view the award of damages as constituting the appropriate remedy for Mrs. Lee.

D. DISPOSITION

159 For these reasons I would set aside the motions judge's order and substitute an order:

1. rescinding Mr. Singh's agreement of purchase and sale;

2. awarding damages to Mrs. Lee as against Talon for negligent misrepresentation;

3. as against Shnaider, Levitan and Trump, dismissing only those of the appellant's claims that were advanced for breach of the OSC Ruling and for misrepresentations;

4. remitting the claim for fraudulent misrepresentation to be decided on a further motion for summary judgment or at trial before the Superior Court;

5. awarding pre and post-judgment interest on the damage awards; and

6. for costs of the appeal on a partial indemnity basis to the appellants as against Talon fixed in the amount of $35,000, inclusive of disbursements and applicable taxes.

160 As the matter is continuing in the Superior Court, I leave that court to decide how Mrs. Lee's damages are to be calculated and fixed as well as to determine what is necessary to implement the order rescinding Mr. Singh's agreement of purchase and sale.

161 If the parties are unable to agree on the costs of the original motions, the appellants shall provide brief written submissions not to exceed three pages within 21 days of the release of these reasons and the respondents are to provide their response not to exceed three pages within 14 days thereafter.

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***K. van Rensburg J.A.*:**

I agree

***M.L. Benotto J.A.*:**

I agree

Appeal allowed.

Footnotes

1 The motions judge's reasons show Mrs. Lee's increase to be $2,156.73 or 62% (at para. 165). Those figures appear to be in error and I have used the correct figures.

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TAB 8

2001 SCC 79, 2001 CSC 79
Supreme Court of Canada

Cooper v. Hobart

2001 CarswellBC 2502, 2001 CarswellBC 2503, 2001 SCC 79, 2001 CSC 79, [2001] 3 S.C.R. 537, [2001] B.C.W.L.D. 1084, [2001] S.C.J. No. 76, [2001] B.C.T.C. 215, [2002] 1 W.W.R. 221, 110 A.C.W.S. (3d) 943, 160 B.C.A.C. 268, 206 D.L.R. (4th) 193, 261 W.A.C. 268, 277 N.R. 113, 8 C.C.L.T. (3d) 26, 96 B.C.L.R. (3d) 36, J.E. 2001-2153, REJB 2001-26862

Mary Francis Cooper, Appellant v. Robert J. Hobart and Her Majesty the Queen in right of the Province of British Columbia, Respondents and The Attorney General of Canada, the Attorney General for Ontario, the Attorney General for New Brunswick, Her Majesty the Queen in right of Alberta, the Minister of Justice and the Attorney General for Alberta, the British Columbia Securities Commission, the Ontario Securities Commission, and the Alberta Securities Commission, Interveners

McLachlin C.J.C, Gonthier, Major, Bastarache, Binnie, Arbour, LeBel JJ.

Heard: June 20, 2001
Judgment: November 16, 2001
Docket: 27880

Proceedings: affirming 2000 BCCA 151, 2000 CarswellBC 475, 184 D.L.R. (4th) 287, 75 B.C.L.R. (3d) 54, 49 C.C.L.T. (2d) 148, [2000] 6 W.W.R. 8, 135 B.C.A.C. 266, 221 W.A.C. 266 (B.C. C.A.); reversing 1999 CarswellBC 620, 68 B.C.L.R. (3d) 274 (B.C. S.C.); additional reasons at 1999 CarswellBC 1300, 68 B.C.L.R. (3d) 293, 35 C.P.C. (4th) 124 (B.C. S.C.); and reversing 1999 CarswellBC 1300, 68 B.C.L.R. (3d) 293, 35 C.P.C. (4th) 124 (B.C. S.C.)

Counsel: *David P. Church* , *Andrew J. Pearson* , *Ian G. Schildt* , for Appellant
D. Clifton Prowse , *Karen Horsman* , *Keith L. Johnston* , for Respondents
Donald J. Rennie , for Intervener, Attorney General of Canada
Sara Blake , for Intervener, Attorney General for Ontario
Written submissions only by *Cedric L. Haines, Q.C.* , for Intervener, Attorney General for New Brunswick
Tim Hurlburt , for Interveners, Her Majesty the Queen in right of Alberta, Minister of Justice, and Attorney General for Alberta
James A. Sasha Angus , *Lorne Herlin* , for Intervener, British Columbia Securities Commission
Neil Finkelstein , *Johanna M. Superina* , for Interveners, Ontario Securities Commission and Alberta Securities Commission

Subject: Torts; Civil Practice and Procedure; Public

APPEAL by plaintiff from judgment reported at 2000 BCCA 151, 2000 CarswellBC 475, (sub nom. *Cooper v. British Columbia (Registrar of Mortgage Brokers))* 184 D.L.R. (4th) 287, 75 B.C.L.R. (3d) 54, 49 C.C.L.T. (2d) 148, [2000] 6 W.W.R. 8, (sub nom. *Cooper v. Registar of Mortgage Brokers (B.C.))* 135 B.C.A.C. 266, (sub nom. *Cooper v. Registar of Mortgage Brokers (B.C.))* 221 W.A.C. 266 (B.C. C.A.), allowing appeal by registrar of mortgage brokers and Crown from granting of application by plaintiff for certification of action as class proceeding.

POURVOI de la demanderesse à l'encontre du jugement publié à 2000 BCCA 151, 2000 CarswellBC 475, (sub nom. *Cooper v. British Columbia (Registrar of Mortgage Brokers))* 184 D.L.R. (4th) 287, 75 B.C.L.R. (3d) 54, 49 C.C.L.T.

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(2d) 148, [2000] 6 W.W.R. 8, (sub nom. *Cooper v. Registar of Mortgage Brokers (B.C.))* 135 B.C.A.C. 266, (sub nom. *Cooper v. Registar of Mortgage Brokers (B.C.))* 221 W.A.C. 266 (B.C. C.A.) , qui a accueilli le pourvoi du registrateur des courtiers en hypothèques et de la Couronne à l'encontre de l'accueil de la demande de certification présentée par la demanderesse pour obtenir la certification de son action en tant que recours collectif.

The judgment of the court was delivered by The Chief Justice, *McLachlin C.J.C.* and *Major J.*:

1 The present appeal revisits the *Anns* test (from *Anns v. Merton London Borough Council* (1977), [1978] A.C. 728 (U.K. H.L.)) and, in particular, highlights and hones the role of policy concerns in determining the scope of liability for negligence. The appellant is an investor who alleges that the Registrar of Mortgage Brokers, a statutory regulator, is liable in negligence for failing to oversee the conduct of an investment company which the Registrar licensed. The question is whether the Registrar owes a private law duty of care to members of the investing public giving rise to liability in negligence for economic losses that the investors sustained. Such a duty of care is as yet unrecognized by Canadian courts. For the reasons that follow, we find that this is not a proper case in which to recognize a new duty of care. In the course of these reasons, we attempt to clarify the distinctive policy considerations which impact each stage of the *Anns* analysis.

1. Facts

2 Eron Mortgage Corporation ("Eron") was registered as a mortgage broker under the *Mortgage Brokers Act* , R.S.B.C. 1996, c. 313 ("the Act"), from early 1993 until 1997. On October 3, 1997, the respondent, Robert J. Hobart, in his capacity as the Registrar under the Act ("the Registrar"), suspended Eron's mortgage broker's licence and issued a freeze order in respect of its assets.

3 Eron acted as a mortgage broker for large syndicated loans. It arranged for numerous lenders (or investors) to pool their funds for the purpose of making a single loan to a borrower, which was typically a developer of commercial real estate. The syndicated loans were made in the name of Eron or one of its related companies, which held the security in trust for the investors.

4 It is alleged that the funds provided by the investors were used by Eron for several unauthorized purposes, such as funding interest payments on other non-performing mortgages and paying for personal items for the benefit of the principals of Eron. It is currently estimated that $222 million is outstanding to the investors on these loans. Investors will likely realize only $40 million from the security taken from the loans, leaving a shortfall of $182 million.

5 Soon after Eron's mortgage licence was suspended, it went out of business. The appellant Mary Francis Cooper ("Cooper"), one of over 3000 investors who advanced money to Eron, brought an action against the Registrar. The Statement of Claim alleged that the Registrar breached the duty of care that he allegedly owed to the appellant and other investors. The appellant asserted that by August 28, 1996, the Registrar was aware of serious violations of the Act committed by Eron but that he failed to suspend Eron's mortgage broker's licence until October 3, 1997 and failed to notify investors that Eron was under investigation by the Registrar's office. According to the appellant, if the Registrar had taken steps to suspend or cancel Eron's mortgage broker's licence at an earlier date, the losses suffered by the investors would have been avoided or diminished.

6 The appellant applied to have the action certified as a class proceeding under the *Class Proceedings Act* , R.S.B.C. 1996, c. 50. Pursuant to s. 4(1)(a), in order to certify an action as a class proceeding, a court must first determine whether the pleadings disclose a cause of action. The cause of action alleged in the Statement of Claim is negligence which requires, among other things, that a duty of care in tort law be owed by the Registrar to the appellant investor. Therefore, the question was whether the Registrar of Mortgage Brokers, a statutory regulator, owes a private law duty of care to members of the investing public for alleged negligence in failing to properly oversee the conduct of an investment company licensed by the regulator.

2. Judicial History

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1. British Columbia Supreme Court (1999), 68 B.C.L.R. (3d) 274 (B.C. S.C.)

7 Tysoe J. held that the plaintiffs should be permitted to bring a class action. He applied the test cited in *Endean v. Canadian Red Cross Society* (1998), 48 B.C.L.R. (3d) 90 (B.C. C.A.) that unless it is plain and obvious that no reasonable cause of action is disclosed, the plaintiff will have met the requirement set out in s. 4(1)(a) of the *Class Proceedings Act* that there is a cause of action.

8 In determining whether there was clearly no cause of action, the trial judge turned to the test set out by the House of Lords in *Anns* as restated by the British Columbia Court of Appeal in *Dorman Timber Ltd. v. British Columbia* (1997), 40 B.C.L.R. (3d) 230 (B.C. C.A.) , at p. 247:

> (a) Should the defendant have foreseen that damage was likely to result from the negligent action? If yes, then there is a *prima facie* duty of care.
>
> (b) Are there any considerations which would negative or limit the *prima facie* duty of care?

9 The trial judge answered the first question in the affirmative, as the Registrar would have reasonably contemplated that carelessness on his part was likely to cause damage to the plaintiff, a person dealing with a mortgage broker. He went on to answer the second question in the negative, holding that there were no considerations negativing or limiting the *prima facie* duty of care on the basis of four sub-questions:

> 1) Was the defendant's action the result of a policy decision of a public body?
>
> 2) Is the defendant protected by statute or the common law?
>
> 3) Is the defendant exempted from liability by a 'good faith' clause in a statute?
>
> 4) Is the relationship between the parties so distant and tenuous, or is the plaintiff unknown to the defendant, so that it can be said that to impose liability would be unjust?

10 The trial judge found that, in order to answer the first three sub-questions, an appreciation of the "full factual matrix" would be required. Therefore, a trial was needed. The fourth sub-question raised the potential problem of indeterminate liability. The trial judge stated that the prospect of indeterminate liability should negative the *prima facie* duty of care unless it is determined that one of the purposes of the Legislature in enacting the Act was to protect a class of persons, of which the plaintiff is a member. He concluded that it was not plain and obvious that the Legislature did not intend to create a private law duty of care owed by the Registrar in favour of investors dealing with mortgage brokers. In reaching this conclusion, the trial judge referred to various powers and duties of the Registrar which suggested that the Act was intended to protect investors.

11 The trial judge concluded that the pleadings disclosed a cause of action. On June 10, 1999, he certified the action as a class proceeding and stayed the third party proceedings until the conclusion of the trial on the common issues.

2. British Columbia Court of Appeal 75 B.C.L.R. (3d) 54, 2000 BCCA 151 (B.C. C.A.)

12 The Court of Appeal reversed the trial judge's decision, holding that the pleadings did not disclose a cause of action against the Registrar.

(1) Newbury J.A. (Southin J.A. concurring)

13 Newbury J.A. for the majority considered the *Anns* test as it was applied by the Supreme Court of Canada in *Nielsen v. Kamloops (City)*, [1984] 2 S.C.R. 2 (S.C.C.) . First, "is there a 'sufficient relationship of proximity or neighbourhood' such that, in the reasonable contemplation of the Registrar, carelessness on his part might be likely to cause damage to

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the latter; and if so, are there considerations that ought to negative, reduce or limit the scope of the duty or the class of persons to whom it is owed or the damages to which it may give rise?" (para. 32).

14 Under the first branch of the *Anns /Kamloops (City)* test, Newbury J.A. was not satisfied that the test for a *prima facie* duty of care was met. Even though the Registrar might reasonably have foreseen that losses to investors would result if he was careless in carrying out his duties under the Act, it cannot be said that there was a sufficiently close relationship between the parties. In fact, according to Newbury J.A., there was "no 'relationship'" between the plaintiff Cooper and the Registrar as the plaintiff was not even aware of the Registrar's existence.

15 Newbury J.A. turned to the second branch of the *Anns /Kamloops (City)* test in the event that she erred on the first branch of the test. She concluded that there are substantial factors that militate against finding a duty of care in this case. Specifically, the statutory scheme was not intended to create a private law duty of care owed by the Registrar to investors. If it were otherwise, the potential liability would be virtually indeterminate given that the Act imposed no limit on, and the Registrar had no means of controlling, the number of persons who could invest or lend money via a mortgage broker or the amount of money that could be advanced.

(2) Huddart J.A.

16 While Huddart J.A. agreed with the result reached by Newbury J.A., she approached the conclusion from a slightly different perspective. The starting point for her analysis was the nature of the Registrar's office, an office created and defined by statute.

17 The Registrar's responsibilities under the Act require him to make difficult discretionary decisions in the public interest. The public interest is not synonymous with the interest of investors. The Registrar's decisions must be "multi-factorial", taking into account various interests.

18 The question to be answered was whether the Act itself indicates that the taxpayers through their elected representatives agreed to be responsible for private loss to persons in the situation of the investors. Huddart J.A. could not find that intention in the Act, particularly in the face of s. 20 which precludes an action against the Registrar for the performance of duties under the Act or Regulations "unless it was done in bad faith" (para. 82).

19 Huddart J.A. concluded that the only duty that the Registrar owed to the plaintiff Cooper was the duty to exercise due care in ascertaining the scope of his authority (from *Comeau's Sea Foods Ltd. v. Canada (Minister of Fisheries & Oceans)*, [1997] 1 S.C.R. 12 (S.C.C.) , at paras. 52-54). He interpreted his statutory authority correctly.

3. Issue

20 Does a statutory regulator owe a private law duty of care to members of the investing public for (alleged) negligence in failing to properly oversee the conduct of an investment company licensed by the regulator?

4. Analysis

21 Canadian courts have not thus far recognized the duty of care that the appellants allege in this case. The question is therefore whether the law of negligence should be extended to reach this situation. While the particular extension sought is novel, the more general issue of how far the principles of liability for negligence should be extended is a familiar one, and one with which this Court and others have repeatedly grappled since Lord Atkin enunciated the negligence principle in *McAlister (Donoghue) v. Stevenson*, [1932] A.C. 562 (U.K. H.L.) , almost 70 years ago. That case introduced the principle that a person could be held liable only for reasonably foreseeable harm. But it also anticipated that not all reasonably foreseeable harm might be caught. This posed the issue with which courts still struggle today: to what situations does the law of negligence extend? This case, like so many of its predecessors, may thus be seen as but a gloss on the case of *McAlister (Donoghue) v. Stevenson* .

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22 In *McAlister (Donoghue) v. Stevenson* the House of Lords revolutionized the common law by replacing the old categories of tort recovery with a single comprehensive principle — the negligence principle. Henceforward, liability would lie for negligence in circumstances where a reasonable person would have viewed the harm as foreseeable. However, foreseeability alone was not enough; there must also be a close and direct relationship of proximity or neighbourhood.

23 But what is proximity? For the most part, lawyers apply the law of negligence on the basis of categories as to which proximity has been recognized in the past. However, as Lord Atkin declared in *McAlister (Donoghue) v. Stevenson* , the categories of negligence are not closed. Where new cases arise, we must search elsewhere for assistance in determining whether, in addition to disclosing foreseeability, the circumstances disclose sufficient proximity to justify the imposition of liability for negligence.

24 In *Anns* , *supra* , at pp. 751-52, the House of Lords, *per* Lord Wilberforce, said that a duty of care required a finding of proximity sufficient to create a *prima facie* duty of care, followed by consideration of whether there were any factors negativing that duty of care. This Court has repeatedly affirmed that approach as appropriate in the Canadian context.

25 The importance of *Anns* lies in its recognition that policy considerations play an important role in determining proximity in new situations. Long before *Anns* , courts in Canada and elsewhere had recognized that the decision of how far to extend liability for negligence involved policy considerations. As H. Street put it in *The Law of Torts* (6th ed. 1976), at p.108, citing a Canadian case, *Nova Mink Ltd. v. Trans Canada Airlines*, [1951] 2 D.L.R. 241 (N.S. C.A.) , at pp. 254-55:

> ... it cannot be too strongly stressed that the use of [the] test of foreseeability in order to determine whether there is a duty-relationship between the parties conceals the true judicial process — that test is in fact a conclusion embracing within it, and yet concealing the identity of, the several considerations of policy, and the balancing of interests which have led the court to decide that a duty is owed.

26 The House of Lords in *Anns* for the first time expressly recognized the policy component in determining the extension of the negligence principle. However, it left doubt on the precise content of the first and second branches of the new formulation of the negligence principle. This gave rise to debate — debate which the submissions in this case revive. Was the first branch concerned with foreseeability only or foreseeability and proximity? If the latter, was there duplication between policy considerations relevant to proximity at the first stage and the second stage of the test?

27 To some extent, these concerns are academic. Provided the proper balancing of the factors relevant to a duty of care are considered, it may not matter, so far as a particular case is concerned, at which "stage" it occurs. The underlying question is whether a duty of care should be imposed, taking into account all relevant factors disclosed by the circumstances. *Anns* did not purport to depart from the negligence test of *McAlister (Donoghue) v. Stevenson* but merely sought to elucidate it by explicitly recognizing its policy component.

28 We continue in the view, repeatedly expressed by this Court, that the *Anns* two-stage test, properly understood, does not involve duplication because different types of policy considerations are involved at the two stages. In our view, *Anns* continues to provide a useful framework in which to approach the question of whether a duty of care should be imposed in a new situation.

29 Nevertheless, it is important from the point of view of methodology and clarity in the law to be clear on what falls to be considered at each stage of the *Anns* test. In this connection, it is useful to consider the leading English case on that question. The Judicial Committee of the Privy Council held in *Yuen Kun Yeu v. Hong Kong (Attorney General)* (1987), [1988] A.C. 175 (Hong Kong P.C.) , that to find a *prima facie* duty of care at the first stage of the test there must be reasonable foreseeability of the harm plus something more. As will be seen, we agree with this conclusion. The Privy Council went on to opine that *Anns* ' second branch, negation for policy reasons, would seldom come into play. If this is read as a suggestion that policy is not important in determining whether the negligence principle should be extended to new situations, we would respectfully differ. As Street points out, the *McAlister (Donoghue) v. Stevenson* foreseeability-

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negligence test, no matter how it is phrased, conceals a balancing of interests. The quest for the right balance is in reality a quest for prudent policy. The difference in the two positions, if there is one, may turn on how one defines policy; the Privy Council in *Yuen Kun Yeu* appears to regard policy as confined to practical considerations dictating immunity despite a close relationship and foreseeability.

30 In brief compass, we suggest that at this stage in the evolution of the law, both in Canada and abroad, the *Anns* analysis is best understood as follows. At the first stage of the *Anns* test, two questions arise: (1) was the harm that occurred the reasonably foreseeable consequence of the defendant's act? and (2) are there reasons, notwithstanding the proximity between the parties established in the first part of this test, that tort liability should not be recognized here? The proximity analysis involved at the first stage of the *Anns* test focuses on factors arising from the *relationship* between the plaintiff and the defendant. These factors include questions of policy, in the broad sense of that word. If foreseeability and proximity are established at the first stage, a *prima facie* duty of care arises. At the second stage of the *Anns* test, the question still remains whether there are residual policy considerations outside the relationship of the parties that may negative the imposition of a duty of care. It may be, as the Privy Council suggests in *Yuen Kun Yeu* , that such considerations will not often prevail. However, we think it useful expressly to ask, before imposing a new duty of care, whether despite foreseeability and proximity of relationship, there are other policy reasons why the duty should not be imposed.

31 On the first branch of the *Anns* test, reasonable foreseeability of the harm must be supplemented by proximity. The question is what is meant by proximity. Two things may be said. The first is that "proximity" is generally used in the authorities to characterize the type of relationship in which a duty of care may arise. The second is that sufficiently proximate relationships are identified through the use of categories. The categories are not closed and new categories of negligence may be introduced. But generally, proximity is established by reference to these categories. This provides certainty to the law of negligence, while still permitting it to evolve to meet the needs of new circumstances.

32 On the first point, it seems clear that the word "proximity" in connection with negligence has from the outset and throughout its history been used to describe the type of relationship in which a duty of care to guard against foreseeable negligence may be imposed. "Proximity" is the term used to describe the "close and direct" relationship that Lord Atkin described as necessary to grounding a duty of care in *McAlister (Donoghue) v. Stevenson* , *supra* , at pp. 580-81:

> Who then, in law, is my neighbour? The answer seems to be — persons who are so closely and directly affected by my act that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions which are called into question.
>
> .....
>
> I think that this sufficiently states the truth if proximity be not confined to mere physical proximity, but be used, as I think it was intended, to extend to such close and direct relations that the act complained of directly affects a person whom the person alleged to be bound to take care would know would be directly affected by his careless act. [Emphasis added.]

33 As this Court stated in *Hercules Management Ltd. v. Ernst & Young*, [1997] 2 S.C.R. 165 (S.C.C.) at para. 24, *per* La Forest J.:

> The label "proximity", as it was used by Lord Wilberforce in *Anns, supra* , was clearly intended to connote that the circumstances of the relationship inhering between the plaintiff and the defendant are of such a nature that the defendant may be said to be under an obligation to be mindful of the plaintiff's legitimate interests in conducting his or her affairs . [Emphasis added.]

34 Defining the relationship may involve looking at expectations, representations, reliance, and the property or other interests involved. Essentially, these are factors that allow us to evaluate the closeness of the relationship between the

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plaintiff and the defendant and to determine whether it is just and fair having regard to that relationship to impose a duty of care in law upon the defendant.

35 The factors which may satisfy the requirement of proximity are diverse and depend on the circumstances of the case. One searches in vain for a single unifying characteristic. As stated by McLachlin J. (as she then was) in *Canadian National Railway v. Norsk Pacific Steamship Co.*, [1992] 1 S.C.R. 1021 (S.C.C.), at p. 1151: "[p]roximity may be usefully viewed, not so much as a test in itself, but as a broad concept which is capable of subsuming different categories of cases involving different factors" (cited with approval in *Hercules Managements, supra*, at para. 23). Lord Goff made the same point in *Davis v. Radcliffe*, [1990] 2 All E.R. 536 (England P.C.), at p. 540:

> ... it is not desirable, at least in the present stage of the development of the law, to attempt to state in broad general propositions the circumstances in which such proximity may or may not be held to exist. On the contrary, following the expression of opinion by Brennan J in *Sutherland Shire Council v Heyman* (1985) 60 ALR 1 at 43-44, it is considered preferable that 'the law should develop categories of negligence incrementally and by analogy with established categories'.

36 What then are the categories in which proximity has been recognized? First, of course, is the situation where the defendant's act foreseeably causes physical harm to the plaintiff or the plaintiff's property. This has been extended to nervous shock (see, for example, *Alcock v. Chief Constable of South Yorkshire Police*, [1991] 4 All E.R. 907 (U.K. H.L.)). Yet other categories are liability for negligent misstatement: *Hedley Byrne & Co. v. Heller & Partners Ltd.*, [1963] 2 All E.R. 575 (U.K. H.L.), and misfeasance in public office. A duty to warn of the risk of danger has been recognized: *Rivtow Marine Ltd. v. Washington Iron Works* (1973), [1974] S.C.R. 1189 (S.C.C.). Again, a municipality has been held to owe a duty to prospective purchasers of real estate to inspect housing developments without negligence: *Anns*, *supra*; *Kamloops (City)*, *supra*. Similarly, governmental authorities who have undertaken a policy of road maintenance have been held to owe a duty of care to execute the maintenance in a non-negligent manner: *Just v. British Columbia*, [1989] 2 S.C.R. 1228 (S.C.C.), *Swinamer v. Nova Scotia (Attorney General)*, [1994] 1 S.C.R. 445 (S.C.C.), *etc.* Relational economic loss (related to a contract's performance) may give rise to a tort duty of care in certain situations, as where the claimant has a possessory or proprietary interest in the property, the general average cases, and cases where the relationship between the claimant and the property owner constitutes a joint venture: *Norsk Pacific Steamship Co.*, *supra*; *Bow Valley Husky (Bermuda) Ltd. v. Saint John Shipbuilding Ltd.*, [1997] 3 S.C.R. 1210 (S.C.C.). When a case falls within one of these situations or an analogous one and reasonable foreseeability is established, a *prima facie* duty of care may be posited.

37 This brings us to the second stage of the *Anns* test. As the majority of this Court held in *Norsk Pacific Steamship Co.*, at p. 1155, residual policy considerations fall to be considered here. These are not concerned with the relationship between the parties, but with the effect of recognizing a duty of care on other legal obligations, the legal system and society more generally. Does the law already provide a remedy? Would recognition of the duty of care create the spectre of unlimited liability to an unlimited class? Are there other reasons of broad policy that suggest that the duty of care should not be recognized? Following this approach, this Court declined to find liability in *Hercules Managements*, supra, on the ground that to recognize a duty of care would raise the spectre of liability to an indeterminate class of people.

38 It is at this second stage of the analysis that the distinction between government policy and execution of policy falls to be considered. It is established that government actors are not liable in negligence for policy decisions, but only operational decisions. The basis of this immunity is that policy is the prerogative of the elected Legislature. It is inappropriate for courts to impose liability for the consequences of a particular policy decision. On the other hand, a government actor may be liable in negligence for the manner in which it executes or carries out the policy. In our view, the exclusion of liability for policy decisions is properly regarded as an application of the second stage of the *Anns* test. The exclusion does not relate to the relationship between the parties. Apart from the legal characterization of the government duty as a matter of policy, plaintiffs can and do recover. The exclusion of liability is better viewed as an immunity imposed because of considerations outside the relationship for policy reasons — more precisely, because it is inappropriate for courts to second-guess elected legislators on policy matters. Similar considerations may arise where the decision in question is quasi-judicial (see *Edwards v. Law Society of Upper Canada*, 2001 SCC 80 (S.C.C.)).

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39 The second step of *Anns* generally arises only in cases where the duty of care asserted does not fall within a recognized category of recovery. Where it does, we may be satisfied that there are no overriding policy considerations that would negative the duty of care. In this sense, I agree with the Privy Council in *Yuen Kun Yeu* that the second stage of *Anns* will seldom arise and that questions of liability will be determined primarily by reference to established and analogous categories of recovery. However, where a duty of care in a novel situation is alleged, as here, we believe it necessary to consider both steps of the *Anns* test as discussed above. This ensures that before a duty of care is imposed in a new situation, not only are foreseeability and relational proximity present, but there are no broader considerations that would make imposition of a duty of care unwise.

VI. Application of the Test

40 The appellants submit that the Registrar of Mortgage Brokers owed them, as investors with a firm falling under the Registrar's administrative mandate, a duty of care giving rise to liability for negligence and damages for losses that they sustained. The investors allege that the Registrar should have acted earlier to suspend Eron or warn them of Eron's breaches of the Act's requirements, and that their losses are traceable to the Registrar's failure to act more promptly.

41 The first question is whether the circumstances disclose reasonably foreseeable harm and proximity sufficient to establish a *prima facie* duty of care. The first inquiry at this stage is whether the case falls within or is analogous to a category of cases in which a duty of care has previously been recognized. The answer to this question is no.

42 The next question is whether this is a situation in which a new duty of care should be recognized. It may be that the investors can show that it was reasonably foreseeable that the alleged negligence in failing to suspend Eron or issue warnings might result in financial loss to the plaintiffs. However, as discussed, mere foreseeability is not enough to establish a *prima facie* duty of care. The plaintiffs must also show proximity — that the Registrar was in a close and direct relationship to them making it just to impose a duty of care upon him toward the plaintiffs. In addition to showing foreseeability, the plaintiffs must point to factors arising from the circumstances of the relationship that impose a duty.

43 In this case, the factors giving rise to proximity, if they exist, must arise from the statute under which the Registrar is appointed. That statute is the only source of his duties, private or public. Apart from that statute, he is in no different position than the ordinary man or woman on the street. If a duty to investors with regulated mortgage brokers is to be found, it must be in the statute.

44 In this case, the statute does not impose a duty of care on the Registrar to investors with mortgage brokers regulated by the Act. The Registrar's duty is rather to the public as a whole. Indeed, a duty to individual investors would potentially conflict with the Registrar's overarching duty to the public.

45 A brief review of the relevant powers and duties of the Registrar under the Act confirms this conclusion. Part I sets out the Registrar's regulatory powers with respect to the operation of mortgage brokers and submortgage brokers in British Columbia. Specifically, s. 4 provides that the Registrar must grant registration or renewal of registration to an applicant if, in his opinion, the applicant is "suitable" for registration and the proposed registration is "not objectionable". He may also attach such conditions and restrictions to the registration as he considers necessary. Once registered, a mortgage broker must comply with s. 6 of the Regulations which mandates that registrants maintain proper books and records and file annual financial statements with the Registrar.

46 Sections 5 and 6 of the Act cover the investigatory powers of the Registrar. Pursuant to s. 5, the Registrar may, and on receipt of a sworn complaint must, investigate any matter arising out of the Act or Regulations. In pursuit of this purpose, the Registrar may examine any records and documents of the person being investigated. He may summon witnesses and compel them to give evidence on oath or otherwise and to produce records, property, assets or things in the same manner as the court does for the trial of civil actions. Section 7 allows the Registrar to "freeze" funds or securities where he has made or is about to make a direction, decision, order or ruling suspending or cancelling the registration

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of a person under the Act. He may also apply to the court for an appointment of a receiver, or a receiver and manager, or trustee of the property of the person.

47 Under s. 8, the Registrar may, after giving a person registered under the Act an opportunity to be heard, suspend or cancel any registration if, in his opinion, any of the following or other conditions apply: the person would be disentitled to registration if the person were an applicant under s. 4; the person is in breach of a condition of registration; the person is a party to a mortgage transaction which is harsh and unconscionable or otherwise inequitable; or the person has conducted or is conducting business in a manner that is otherwise prejudicial to the public interest. Section 14 prohibits a broker from making any false, misleading or deceptive statements in any advertisement, circular or similar material. Part II of the Act is directed towards the protection of borrowers, investors and lenders, mandating in part specific disclosure requirements by mortgage lenders and their agents. Section 8 of the Regulations provides that every direction, decision, order or ruling of the Registrar refusing registration, refusing to renew registration, suspending registration or cancelling registration shall be made in writing and shall be open to public inspection.

48 Finally, s. 20 exempts the Registrar or any person acting under his authority from any action brought for anything done in the performance of duties under the Act or Regulations, or in pursuance or intended or supposed pursuance of the Act or Regulations, unless it was done in bad faith.

49 The regulatory scheme governing mortgage brokers provides a general framework to ensure the efficient operation of the mortgage marketplace. The Registrar must balance a myriad of competing interests, ensuring that the public has access to capital through mortgage financing while at the same time instilling public confidence in the system by determining who is "suitable" and whose proposed registration as a broker is "not objectionable". All of the powers or tools conferred by the Act on the Registrar are necessary to undertake this delicate balancing. Even though to some degree the provisions of the Act serve to protect the interests of investors, the overall scheme of the Act mandates that the Registrar's duty of care is not owed to investors exclusively but to the public as a whole.

50 Accordingly, we agree with the Court of Appeal *per* Newbury J.A.: even though the Registrar might reasonably have foreseen that losses to investors in Eron would result if he was careless in carrying out his duties under the Act, there was insufficient proximity between the Registrar and the investors to ground a *prima facie* duty of care. The statute cannot be construed to impose a duty of care on the Registrar specific to investments with mortgage brokers. Such a duty would no doubt come at the expense of other important interests, of efficiency and finally at the expense of public confidence in the system as a whole.

51 Having found no proximity sufficient to found a duty of care owed by the Registrar to the investors, we need not proceed to the second branch of the *Anns* test and the question of whether there exist policy considerations apart from those considered in determining a relationship of proximity, which would negative a *prima facie* duty of care, had one been found. However, the matter having been fully argued, it may be useful to comment on those submissions.

52 In our view, even if a *prima facie* duty of care had been established under the first branch of the *Anns* test, it would have been negated at the second stage for overriding policy reasons. The decision of whether to suspend a broker involves both policy and quasi-judicial elements. The decision requires the Registrar to balance the public and private interests. The Registrar is not simply carrying out a pre- determined government policy, but deciding, as an agent of the executive branch of government, what that policy should be. Moreover, the decision is quasi-judicial. The Registrar must act fairly or judicially in removing a broker's licence. These requirements are inconsistent with a duty of care to investors. Such a duty would undermine these obligations, imposed by the Legislature on the Registrar. Thus even if a *prima facie* duty of care could be posited, it would be negated by other overriding policy considerations.

53 The *prima facie* duty of care is also negated on the basis of the distinction between government policy and the execution of policy. As stated, the Registrar must make difficult discretionary decisions in the area of public policy, decisions which command deference. As Huddart J.A. (concurring in the result) found, the decisions made by the Registrar were made within the limits of the powers conferred upon him in the public interest.

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54 Further, the spectre of indeterminate liability would loom large if a duty of care was recognized as between the Registrar and investors in this case. The Act itself imposes no limit and the Registrar has no means of controlling the number of investors or the amount of money invested in the mortgage brokerage system.

55 Finally, we must consider the impact of a duty of care on the taxpayers, who did not agree to assume the risk of private loss to persons in the situation of the investors. To impose a duty of care in these circumstances would be to effectively create an insurance scheme for investors at great cost to the taxpaying public. There is no indication that the Legislature intended that result.

56 In the result the judgment of the British Columbia Court of Appeal is affirmed and the appeal is dismissed with costs.

Appeal dismissed.

Pourvoi rejeté.

End of Document

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TAB 9

1997 CarswellBC 925
British Columbia Court of Appeal

Kripps v. Touche Ross & Co.

1997 CarswellBC 925, [1997] 6 W.W.R. 421, [1997] B.C.J. No. 968, 145 W.A.C. 288,
33 B.C.L.R. (3d) 254, 35 C.C.L.T. (2d) 60, 70 A.C.W.S. (3d) 931, 89 B.C.A.C. 288

Stephen Kripps, Agnes Kripps, Edward Thorpe, Bonnie Thorpe, David Plunz and Gayle Plunz, Plaintiffs (Appellants) and Touche Ross & Co., Defendant (Respondent) and Victoria Mortgage Corporation Ltd., Oakside Corporation Ltd., Hermann G. Bessert, Robert E. Mitchell, Hugh M. Blair, Daniel P. Kramer, James D. Kadlec and Douglas T. Hawkes, Defendants

Rowles, Finch and Ryan JJ.A.

Heard: June 11-13, 1996
Judgment: April 25, 1997
Docket: Vancouver CA019919

Proceedings: **Proceedings: reversing (1995), 5 B.C.L.R. (3d) 22 (B.C.S.C.)**

Counsel: *G.A. Urquhart, Q.C.*, and *D.A. Brindle*, for Appellants.
W.B. McAllister, Q.C., and *N. Garson*, for Respondent.

Subject: Torts; Public; Contracts; Corporate and Commercial

APPEAL by plaintiffs from judgment reported at 5 B.C.L.R. (3d) 22, [1995] 6 W.W.R. 180, 24 C.C.L.T. (2d) 136, 22 B.L.R. (2d) 86 (S.C.), dismissing action for damages for negligent misrepresentation.

***Finch J.A.* (*Rowles J.A.* concurring):**

I

1 This appeal is from the judgment of Mr. Justice Lowry, pronounced 30 January 1995 in the Supreme Court of British Columbia, which dismissed the plaintiffs' action for economic loss *simpliciter* for negligent misrepresentation or non-disclosure by the defendant auditors. The decision is reported at (1995), 5 B.C.L.R. (3d) 22, [1995] 6 W.W.R. 180 (B.C. S.C.), and (1995), 24 C.C.L.T. (2d) 136 (B.C. S.C.).

II Facts

2 The plaintiffs are investors who purchased debentures after the issue of a prospectus by Victoria Mortgage Corporation Ltd. ("VMCL") on 24 September 1984.

3 VMCL was at all material times owned by Oakside Corporation Limited, a private holding company of Hermann Bessert. The company's primary business was providing loans secured by mortgages on real property. The mortgages held by VMCL were its principal asset, and interest from those mortgages was its main source of income. VMCL borrowed money by selling fixed-term debentures which were offered to the public on a continuous basis. The borrowed money was then loaned against mortgage security in real estate. Subject only to the company's bank debt, the debentures constituted a first priority charge on its assets. VMCL's success depended upon making a profit by maintaining the spread between the interest rate it paid to debenture holders and the interest rate it earned on its mortgage loans.

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4 VMCL's policy, as expressed in the notes to its financial statements, was to "capitalize" accrued interest on mortgages in default, if the company's management believed those amounts to be adequately secured. So, where mortgage payments were in arrears, the unpaid interest was added to the principal value of the mortgage. At the same time the uncollected interest was included in VMCL's statement of income. The learned trial judge found that the company policy with respect to capitalizing unpaid interest was consistent with Generally Accepted Accounting Principles (GAAP) applicable during the relevant period. The amount of unpaid interest capitalized in the financial statements was disclosed in publicly-available accounts filed quarterly with the Superintendent of Brokers.

5 VMCL recognized the risk that some unpaid interest might never be recovered. This was accounted for in VMCL's financial statements by a provision for investment loss. One of the issues in this case is whether the loss provision in the audited 1983 financial statements was adequate.

6 The *Securities Act*, R.S.B.C. 1979, c. 380 (subsequently replaced by S.B.C. 1985, c. 83) prohibited the sale of debentures to the public unless, annually, a prospectus was filed with the Superintendent of Brokers and given to prospective purchasers. The *Act* required that the prospectus include financial statements and an auditor's report. Section 42 of the *Act* required that this auditor's report state that the financial statements presented the financial position of the company fairly according to GAAP, and that otherwise the report be unqualified. The *Act* also required the company to obtain and file the written consent of its auditor to the use of its report, which consent had to state that the auditor had read the prospectus and that the information derived from the financial statements in the prospectus or within the auditor's knowledge was presented fairly and was not misleading.

7 The defendant Touche was engaged only for the purpose of satisfying the regulatory requirements with respect to the annual prospectus that VMCL had to submit to the Superintendent. The defendant knew that the audits were undertaken to facilitate the sale of VMCL's debentures to the public and that its reports formed part of the prospectus distributed to any prospective purchaser. Walter Brock was the Touche partner in charge of the VMCL audit.

8 Each of the prospectuses issued by VMCL contained a statement of the risk associated with lending money to a company the assets of which are secured by mortgages on real estate, to the effect that, due to the nature of real estate investment portfolios, there was a risk that VMCL might be unable to pay interest or the face value of a debenture.

9 Between November 1983 and March 1984, Mr. Brock, a chartered accountant with 25 years of experience, performed Touche's audit of the 1983 financial statements, and in March 1984, he gave the audit report to VMCL.

10 The plaintiffs claim that in making their decisions to purchase debentures between December 1984 and March 1985 they relied, in part, on Touche's auditor's report of the 1983 financial statements, which was included with those financial statements in the prospectus issued in September 1984.

11 The audit report, completed by the defendant on 15 March 1984, was in the standard form of audit report prescribed by the Canadian Institute of Chartered Accountants. It read in part:

> *In our opinion, these financial statements present fairly the financial position of the Company as at December 31, 1983* and 1982, and the results of its operations and the changes in its financial position for the years ended December 31, 1983, 1982, and 1981, the four month period ended December 31, 1980 and the year ended August 31, 1980 *in accordance with generally accepted accounting principles applied on a consistent basis.*
>
> (emphasis added)

12 The 1983 financial statements of VMCL showed that, as of 31 December 1983, it held first, second, and third mortgages with a total value of approximately $14.3 million. With respect to mortgages in arrears, the learned trial judge made these findings (at para.21):

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> In December, 1983, 14 loans totalling about $3.5 million, or one quarter of the value of the portfolio, were in default for more than 90 days ($2.6 million for more than 12 months). Additionally, the company's largest loan, the balance of which was $1.4 million, would have been in default except that it was renegotiated that month and interest payments were deferred for six months. The total amount of unpaid interest was $729,000 or 40% of the interest earned. The situation had deteriorated since the '82 year end ($3.6 million being one third of the loan balance with interest unpaid being $327,000 or 20% of what was earned).

13 Mr. Brock accepted representations from VMCL's management that disclosure of mortgages in arrears was not required under GAAP. He agreed, ultimately, to sign an auditor's report for financial statements that did not disclose the mortgage arrears.

14 The trial judge held that the amount of mortgages in default was material information that would have given investors a better understanding of the risk involved.

15 The defendant identified 19 mortgages and 1 investment property as being of questionable value and Mr. Brock suggested a loss provision of $400,000. Then, after VMCL provided additional information, Mr. Brock accepted that full recovery was in doubt in respect of only 3 loans, totalling $250,000, and he considered that a loss provision of one-half of that total ($125,000) was "fair and reasonable".

16 He also suggested that the financial statements ought to include some reference to "non-performing loans". Mr. Bessert agreed. The note which Mr. Brock prepared for inclusion in the financial statements was as follows:

> Non-performing investments as at December 31, 1983 were approximately $950,000. The Company's experience has been that most non-performing investments are not subject to losses and that these investments are restored to full productive status. For the five year period ended December 31, 1983, the Company did not experience any material investment losses.

17 With respect to this note the learned trial judge found (at para. 28):

> The term "non-performing" was not defined and it had no generally accepted meaning in accounting terminology. The loan total of $950,000 was in fact the full amount of the three loans (plus some cushion) to which the loss provision related. They were loans in respect of which VMCL had no definite strategy for repayment in the near future. They were considered to be not fully secured.

18 The auditor's report was signed on 15 March 1984. VMCL requested Touche's consent to the use of its report and sent it a copy of a prospectus dated 2 April 1984. The defendant reviewed the document and informed the Superintendent of its consent, including, as required, a statement that to its knowledge the information was fairly presented and not misleading.

19 Following a number of inquiries raised by the Superintendent, VMCL prepared and sent an amended prospectus dated 30 June 1984 to Touche, who again provided its consent.

20 A further amended prospectus was prepared by VMCL. The note with respect to non-performing loans of $950,000 did not appear in the financial statements that formed part of this final prospectus, dated 31 July 1984. In revising the prospectus, VMCL removed the note from the financial statements, relocated it to another part of the prospectus under the heading "Investments", and re-worded it to read:

> Non-performing investments receive immediate attention and are reviewed monthly. The Company's general policy is to commence collection procedures if payments are in arrears for a period of three months unless satisfactory arrangements are made with the client. As at December 31, 1983, non-performing investments were approximately $950,000. Although the Company's experience has been that most non-performing investments are not subject to

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losses and that these investments are restored to full productive status, a provision of $125,000 for future losses was established.

The Company set out in tabular form thereafter its gain or loss experience in the preceding four years.

21 Neither Mr. Brock nor any other member of Touche saw the final version of the prospectus. The defendant was not asked by VMCL to consent to the use of its report for the altered version of the financial statements which omitted the note concerning non-performing loans. Touche was never asked to consent to the July 31 prospectus and did not see the document until it was issued to the public.

22 On 24 September 1984, the 1984 prospectus was issued.

23 The plaintiffs began purchasing VMCL debentures early in 1983 after they had obtained and reviewed the 1982 prospectus, which contained the auditor's report on the 1981 financial statements. The plaintiffs later obtained and reviewed the 1983 prospectus when it was issued in May 1983.

24 The Kripps/Thorpe loan balance often exceeded $1,000,000 and the Plunz balance was at times more than $300,000. The plaintiffs insisted on receiving cheques from VMCL when debentures matured and then, subject to the competitiveness of the rate, they would buy more debentures.

25 In the period between December 1984 and March 1985, the Kripps and Thorpes together bought more than $1.5 million worth of VMCL debentures and the Plunzs bought almost $400,000 worth.

26 In the spring of 1985, Touche determined that the continued viability of VMCL as a going concern was then in doubt and informed VMCL that the standard form of audit report required by the *Securities Act* could not be given. Ultimately, a receiver was appointed and the loan portfolio was liquidated. The recovery for debenture holders was less than thirty cents on the dollar. With interest, the Kripps, Thorpes, and Plunzs lost $1,307,539, $932,100, and $546,420, respectively.

27 In the spring of 1986, this action was commenced against Touche, VMCL, VMCL's directors, and the Superintendent. Neither VMCL nor its directors have taken any part in the proceedings.

28 In 1990, as a result of interlocutory applications, the plaintiffs' action against the Superintendent was dismissed and the action against Touche was confined to instances where the debenture holders could establish actual reliance on the audit reports: see *Kripps v. Touche Ross & Co.* (1992), 69 B.C.L.R. (2d) 62 (B.C. C.A.).

29 At trial, the plaintiffs contended that the defendant's report was a negligent misrepresentation because three elements of VMCL's financial position ought to have been disclosed in the financial statements and were not, namely: (1) an adequate loss provision; (2) the default of a substantial part of VMCL's mortgage loan portfolio; and (3) transactions with a related company.

30 The defendant replied by submitting that disclosure of (1) and (3) was not material and that non-disclosure of (2) was in accordance with GAAP. It further argued that no duty of care was owed to the plaintiffs and that the plaintiffs had not established reasonable reliance. It also pleaded contributory negligence. The non-disclosure of (3) is not at issue on this appeal. The trial judge did not consider it necessary to deal with contributory negligence, and no mention was made of the issue in this appeal.

31 One of the plaintiffs' experts, Mr. Roberts, prepared a report in which he concluded, *inter alia*, that the viability of VMCL was in serious question in 1983 and that a cumulative loss provision for 1982 and 1983 of $1.2 million was required in the 1983 statements. One of Touche's experts, Mr. Selman, concluded that there was no viability question in 1983 and that an appropriate loss provision was $394,500. At trial, the plaintiffs were content to accept Mr. Selman's estimate of a loss provision of $394,500 as a minimum, since it showed the $125,000 loss provision made in the 1983

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statements to be inadequate. The plaintiffs further accepted that it could be assumed that there was no "going concern" issue that the audit of the 1983 statements should have disclosed.

32 The trial judge heard no oral testimony. The plaintiffs had obtained directions permitting the case to be tried on affidavits and expert statements subjected to cross-examination in advance of trial. After hearing counsels' submissions on the evidence and the law, the trial judge reached the following conclusions:

1. there was a special relationship between the defendant and the plaintiffs sufficient to give rise to a duty of care on the former;

2. the financial statements in the released prospectus did not disclose the amount of mortgage loans in default, totalling almost $4.9 million;

3. the information regarding the amount of mortgage loans in default was material;

4. GAAP did not require disclosure of mortgage loans in default and so the defendant had met the standard of care to which it was to be held;

5. the financial statements included a loss provision of $125,000 which should have been stated as at least $394,500 and this amounted to a material misrepresentation;

6. the defendant breached its standard of care in accepting the provision of future losses of only $125,000;

7. the defendant signed the auditor's report which accepted as fair under GAAP the financial statements which contained that misstatement, and it was, therefore, responsible for it; and

8. the plaintiffs failed to prove that they had actually relied upon the misstated loss provision as an inducement for their purchase of debentures, and so their claims failed.

III Issues

33 In this Court, the plaintiffs submit that the trial judge erred in failing to find that the defendant made a negligent misrepresentation as a result of the non-disclosure of the $4.9 million worth of mortgage loans in default and in finding that the plaintiffs had not relied on the audited financial statements.

34 The defendant disagrees with the plaintiffs' submissions and argues further that the trial judge erred in concluding that the representation in respect to the loss provision was a material misrepresentation and in finding that the defendant owed a duty of care to the plaintiffs.

IV Analysis

35 The required elements for a successful claim for negligent misrepresentation are: (1) a duty of care based on a "special relationship" between the parties; (2) a misrepresentation; (3) negligence by the representor in making the misrepresentation; (4) reasonable reliance by the representee on the misrepresentation; and (5) damages to the representee caused by the reliance: see *Queen v. Cognos Inc.*, [1993] 1 S.C.R. 87 (S.C.C.) at 110.

36 I will consider each of these elements in turn.

(1) The duty of care

37 The trial judge concluded that the defendant owed a duty of care to the plaintiffs. He expressed his conclusion in these words (at para. 73):

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I conclude that, because the auditors knew that the purpose for which they were engaged to audit the '83 financial statements of VMCL was to facilitate the sale of debentures to the public through the distribution of the company's prospectus containing their report, there was a proximity of relationship between them and an identifiable class of persons who would obtain a copy of the prospectus upon which they would likely rely. The proximity was clearly sufficient to give rise to a duty of care.

38 This conclusion is within the principles enunciated in such cases as *Hedley Byrne & Co. v. Heller & Partners Ltd.* (1963), [1964] A.C. 465, [1963] 2 All E.R. 575 (U.K. H.L.); *Haig v. Bamford*, [1977] 1 S.C.R. 466 (S.C.C.); *Queen v. Cognos, supra;*, *Edgeworth Construction Ltd. v. N.D. Lea & Associates Ltd.*, [1993] 3 S.C.R. 206 (S.C.C.); and *Rangen Inc. v. Deloitte & Touche* (1994), 95 B.C.L.R. (2d) 182 (B.C. C.A.).

39 The finding of a relationship sufficient to give rise to a duty of care on the defendant's part is not at issue on appeal. Rather, the defendant submits that it did not owe a duty of care in respect of the financial statements included in the prospectus issued 24 September 1984, (a) because it was not asked for, and did not give, its consent to the Superintendent of Brokers for the inclusion of its report in the final form of the prospectus; and (b) because the financial statements were "materially different" from those upon which it had given its opinion, with the deletion of the note on "non-performing investments" and the insertion of a new note elsewhere in the prospectus.

40 For comparative purposes, the text of the two notes are set out together. The original note prepared by the defendant reads:

Non-performing investments as at December 31, 1983 were approximately $950,000. The Company's experience has been that most non-performing investments are not subject to losses and that these investments are restored to full productive status. For the five year period ended December 31, 1983, the Company did not experience any material investment losses.

41 The revised note in the prospectus dated 31 July 1984 and issued 24 September 1984 reads:

Non-performing investments receive immediate attention and are reviewed monthly. The Company's general policy is to commence collection procedures if payments are in arrears for a period of three months unless satisfactory arrangements are made with the client. As at December 31, 1983, non-performing investments were approximately $950,000. Although the Company's experience has been that most non- performing investments are not subject to losses and that these investments are restored to full productive status, a provision of $125,000 for future losses was established.

42 The trial judge did not accept the defendant's argument that it owed no duty of care because it had not filed with the Superintendent a consent to the final form of the prospectus. His reasons refer to the legislative scheme of the *Securities Act* which codifies the requirement for an expert's consent to the use of his or her opinion in a prospectus. The relevant provisions at the time were:

Consents of experts

46. (1) If any solicitor, auditor, accountant, engineer, appraiser or any other person or company whose profession gives authority to a statement made by him is named as having prepared or certified any part of a prospectus or is named as having prepared or certified a report or valuation used in or in connection with a prospectus, the written consent of the person or company to the use of his name as having prepared or certified any part of the prospectus or report or valuation and to the inclusion of the report or valuation shall be filed with the superintendent not later than the time the prospectus is filed.

(2) The superintendent may dispense with the filing of a consent required by subsection (1) if, in his opinion, the filing is impracticable or involves undue hardship.

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(3) The consent of the auditor or accountant referred to in subsection (1) shall refer to his report required by section 42, stating the date of it and the dates of the financial statements on which the reports are made, and shall contain a statement that he has read the prospectus and that the information contained in it, which is derived from the financial statements contained in the prospectus or which is within his knowledge, is, in his opinion, presented fairly and is not misleading.

Further consents

47. *Where any change is proposed to be made in a prospectus that in the opinion of the superintendent materially affects any consent required by section 46, the superintendent may require that a further consent be filed with him before a receipt for the amended prospectus is issued.*

(emphasis added)

43 The defendant acknowledges the discretionary power conferred by the *Securities Act* on the Superintendent of Brokers to dispense with the auditor's consent, but says there is nothing in the *Act* to suggest a continuing liability on the auditor where its consent has been dispensed with. It says the *Act* does not operate to fix an auditor with liability for documents which it has not seen. The defendant points out that although the final version of the prospectus was dated 31 July 1984, it was not in fact issued until 24 September 1984, five months after the date on which the audit was completed. The defendant says that if the auditor's consent had been sought in September 1984, a "going concern" problem may have been revealed and the defendant may have required further disclosure as a precondition to the granting of its consent.

44 In my view, the learned trial judge was correct in his finding that whether the defendant had provided a further consent to the Superintendent did not affect the duty of care arising from the application of the principles of *Queen v. Cognos* to the auditor's report. The defendant provided its auditor's report for inclusion in a prospectus; the knowledge of the purpose of the auditor's report gave rise to the defendant's duty of care to the plaintiffs. I agree with the learned trial judge when he said (at paras.59 & 61):

I consider that when auditors accept an audit engagement knowing its purpose is to facilitate the sale of debentures to the public, their consent to its use for that purpose is implicit. They may expect that they may be asked to put such in writing and to make a statement about the financial information in the prospectus to facilitate the regulatory process, but *they have no right to expect to be consulted before all amendments are made and the final form is accepted by the superintendent. Conceivably, in some circumstances, their consent may not be requested at all.* ... [T]he consent requirement can not be viewed as a kind of second chance for the auditors to satisfy themselves that their audit is sound before it is used for its intended purpose. The purpose of the auditors' consent and their statement on the contents of the prospectus as a whole is only to enable the superintendent to best carry out the purpose of the *Act* ...

(emphasis added)

45 This action involved the common law tort of negligent misrepresentation. At the time of the events giving rise to these proceedings, there was no statutory civil liability for auditors under the *Securities Act*. The present *Securities Act*, S.B.C. 1985, c.83, does provide for such statutory liability. This statutory liability is easier for a plaintiff to prove than at common law: a plaintiff need not establish that the auditor owed a duty of care, that there was reliance on the auditor's report, or that the auditor was negligent (although the auditor has a due diligence defence), but merely that the report contained a misrepresentation. It is for this more onerous statutory liability that it is relevant whether an auditor has filed a consent with the Executive Director of the Securities Commission (as the Superintendent of Brokers is now called). Section 114(1) of the present *Act* provides, in part:

114.(1) Where a prospectus contains a misrepresentation, a person who purchases a security offered by the prospectus during the period of distribution

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(a) shall be deemed to have relied on the misrepresentation if it was a misrepresentation at the time of purchase, and

(b) has a right of action for damages against

(iv) *every person whose consent has been filed as prescribed ...*

(emphasis added)

If the present *Securities Act* applied, and if the plaintiff were proceeding under s.114(1)(b)(iv), the absence of the further consent might be a defence. However, the present *Act* does not apply, and this action was brought under the common law.

46 Alternatively, the defendant alleges several material changes in the financial statements. The most significant of the changes relates to the note concerning non-performing loans. In particular, the defendant says that the relocation of the note out of the financial statements rendered its report inapplicable, and that the changed wording of the relocated note gave a more reassuring tone.

47 The plaintiffs' answer to this argument is that the statement concerning non-performing loans was not substantially changed in its content; that the content of that statement was materially misleading because the term "non-performing investments" was not defined, and because it made no reference to the $4.9 million worth of mortgages over three months in arrears; and that the defendant had prepared its auditor's report for inclusion in the prospectus. At trial, the plaintiffs also submitted that the relocation of the note out of the financial statements did not affect the defendant's liability: that the defendant, as the learned trial judge put it (at para. 105), is "responsible for anything of a financial nature in the whole of the prospectus".

48 The plaintiffs argue that the presence of an earlier consent is a basis for imposing liability on the defendant for the relocated note. That is, since the defendant had provided a consent to the Superintendent stating that all financial information in an earlier draft of the prospectus was fair, then the defendant is liable for all financial information in the final prospectus. This is so even though the note had been deleted from the financial statements which were the subject of the auditor's report. The learned trial judge rejected this argument, and I agree with him. He said (at paras. 106-107):

> Assuming that the note, as it appeared in the prospectus, was misleading, I do not accept that there is any basis on which it could be said that reliance on such was reliance on a representation made by the auditors. To the contrary, their representation, insofar as the debenture holders were concerned, was confined to their report. It cannot be said that a person reading the note in the prospectus would have had any justification for attributing it to the auditors....
>
> If a loss amounting to many millions of dollars is to be brought down on the head of an auditor, it must be on some more compelling basis than a misleading statement in a prospectus that could not be read as the auditor's representation and which was in a form the auditor never even saw....

49 In my view, then, the critical question is whether the deletion of the statement concerning non-performing loans from the financial statements was a material change to the financial statements such that the auditor's report no longer applied.

50 In my opinion, given that "non-performing investments" was never defined-specifically that it was never made clear that "non-performing" loans were different from those on which no payments were being made - the note was materially misleading in its original form in the financial statements. Any warning which might have been found in the statement in its original form was too soft and undefined, and its deletion did not substantially affect the financial statements. It is unlikely that any investor would have chosen not to invest on the basis of the original statement.

51 Therefore, I do not agree with the defendant that the financial statements included in the prospectus were financial statements on which the defendant had not given its opinion. Since the financial statements published in the prospectus

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were materially the same as those on which the auditor's report was based, the minor alterations made do not negate the defendant's duty of care. The defendant assumed the potential risk of reliance by investors on statements which it approved. Acceptance of that risk gives rise to a duty of care: *Rangen, supra*, at 192.

52 The trial judge did not err in holding that the defendant owed a duty of care to any investors who relied on the auditor's report contained in the prospectus issued 24 September 1984.

(2) and (3) A negligently made misrepresentation

53 The issue here is whether the defendant's conduct was in breach of the standard of care. The consideration of whether the statement made by the defendant amounted to a misrepresentation is closely connected with this analysis.

a. Was the failure to disclose the amount of arrears a breach of the standard of care?

54 The facts relating to this issue are set out in the decision of the learned trial judge, at paras.77-78:

> The debenture holders contend that the total amount of all mortgages where no interest had been paid for 90 days (almost $4.9 million) ought to have been disclosed even if some of the interest was not technically due because of the company's agreement to defer payment. They say it ought to have been disclosed in a note to the financial statements much like the note that Mr. Brock actually drew. They contend, in addition, that the total amount of all interest unpaid but capitalized ($729,000) ought to have been disclosed as well either in the Statement of Changes in Financial Position or in a further note. They then say they were misled by the incomplete statement in the prospectus about non-performing loans being $950,000. In the absence of any definition as to what non-performing loans were considered to be, they understood such were all loans that were more than 90 days in arrears and that the total amount of loans in default was then less than $1.0 million. They maintain their having been misled can be attributed to the auditors.
>
> The argument is that, given the amounts involved in relation to the company's assets and revenues, proper disclosure of the loan default was necessary to the appropriate presentation of the company's financial position as required in the circumstances. A substantial portion of the company's assets were non-productive; they were not generating funds to meet its obligations, which were primarily the redemption of debentures. Cash flow was essential to the operation of VMCL and the extent of the default bore directly on the company's liquidity and the quality of its loan portfolio. The debenture holders say the auditors recognized the need for disclosure and proposed that it be made so that, as they said, readers of the financial statements would better understand the nature of the risk inherent in buying debentures. Faced with management's resistance, the auditors wrongly decided it was not necessary and then compounded what was a breach of professional standards by accepting an incomplete and, thus, misleading note in place of what they knew was needed. ...

And at para. 82:

> In 1984, the effect of the application of the policy [GAAP] was that unpaid interest, considered by a company's management to be adequately secured, was treated as income and stated to be revenue. Because it was capitalized, it was also added to the loan balances thereby increasing stated assets. If it was considered not to be secured, a loss provision was to be made but, apart from any loss provision, financial statements prepared on this basis disclosed neither the amount of capitalized interest nor the amount of loans in default. It was not generally accepted as an accounting principle that they should do so. The several audited financial statements of various banks and lending institutions for 1983 that are in evidence make this quite clear; it was not GAAP - not the basis on which financial statements were normally prepared.

55 The trial judge then addressed (at para.83) the question whether "the amount of the interest [and] the amount of the loans in default was so large as to have been clearly material to users of the financial statements".

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56 Although capitalizing unpaid interest was part of GAAP at the time Touche prepared its auditor's report, the accounting profession had begun to recognize the failings inherent in this approach. The Canadian Institute of Chartered Accountants (CICA) appears in retrospect to have been moving towards a recognition that failing to disclose explicitly the amount of unpaid interest made it difficult for financial statements to fulfill the broad aim of presenting fairly the financial position of the company, and that GAAP had to be changed so as to fulfill the broader aim. The financial statements prepared for VMCL the next year (1985) did disclose accrued and unpaid interest, although the CICA did not formally change GAAP until later in 1985.

57 The plaintiffs say that whether GAAP was correctly applied does not conclusively determine the issue of whether the defendant met its standard of care. They point out that there are circumstances in which the application of GAAP could lead to misleading financial statements. They say that following the usual practice of the profession cannot protect the defendant where it knew that the purpose of the financial statements and auditor's report was to encourage decisions to buy VMCL debentures and it knew that the information not disclosed would be material to such decisions. In such circumstances, it is open to a court to find negligence on the facts of a case even if the standard practice has been followed.

58 The defendant says that GAAP provides a consistent method of financial reporting and establishes the professional standard. It argues that, in the case of a professional advisor, the determination as to whether the representor has exercised reasonable care is based on a comparison to an objective professional standard. The trial judge found, says the defendant, that the only standard against which the auditor's opinion can be judged is GAAP. Since the financial statements conformed to GAAP, therefore, the defendant's auditor's report does not breach its duty of care.

59 The defendant also takes the position that it did not make a bald statement that the financial statements presented fairly the financial position of VMCL, but rather that the financial statements presented fairly the financial position *in accordance with GAAP*. As the trial judge said at para. 93, the auditor's report "is, in that sense, a qualified opinion of fair presentation, and the qualification cannot be ignored." On the basis of this 'qualification', it does not seem to be strictly necessary to argue that GAAP should be accepted as the professional standard for a truly unqualified opinion; the auditor's report itself apparently restricts its claims to GAAP.

60 The trial judge held that GAAP was the standard of care not because of its status as the considered standard of the accounting profession but because of the "qualified" nature of all auditor's reports. He held that the defendant could not have refused to sign the standard form auditor's report that stated the financial statements were in accordance with GAAP where that was in fact the case merely because the defendant had some other disagreements with the financial statements. He held at para.85:

> [T]he statements on which auditors report are the company's statements, not the auditors'. They are engaged to express an opinion on the company's representation of its financial position. Here the auditors considered there was a disclosure that would assist prospective debenture holders. They proposed that it be made. The company declined. The auditors could not then insist that the disclosure be made; ultimately, *they could only refuse to give an unqualified report if, in their opinion, the company's statements did not fairly present its financial position in accordance with GAAP without the disclosure.*
>
> (emphasis added)

61 The statement of the defendant that is alleged to be a negligent misrepresentation, and the only statement in the prospectus that purports to be made by the defendant, is the auditor's report:

> In our opinion, these financial statements present fairly the financial position of the Company as at December 31, 1983 and 1982, and the results of its operations and the changes in its financial position for the years ended December 31, 1983, 1982 and 1981, the four month period ended December 31, 1980 and the year ended August 31, 1980 in accordance with generally accepted accounting principles applied on a consistent basis.

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This is based on the form suggested by the CICA Handbook. It is the standard form unqualified auditor's report given in Canada.

62 In my respectful view, the statement that "financial statements present fairly the financial position of the company in accordance with generally accepted accounting principles" is ambiguous. It is neither a clear statement of opinion by the professional auditor that the financial statements present fairly the financial position of the company, nor that the financial statements are in accordance with generally accepted accounting principles. In the case at bar, the defendant argued that while the financial statements may present unfairly the financial position of the company (i.e., misrepresent that position), they are nevertheless in accordance with GAAP. Therefore, the defendant says, it is true to say that the financial statements present fairly the financial position according to GAAP. Therefore, it has made no misrepresentation in its auditor's report and is not liable.

63 In my view, the critical issue is the effect of the auditor's report. The learned trial judge concluded that the failure to disclose the amount of arrears was an omission of a piece of material information, but that the capitalization of unpaid interest was the universal practice at the time and was in accordance with GAAP. He therefore concluded that since the capitalization of arrears was in accordance with GAAP, the defendant could not refuse to sign the standard form of auditor's report, regardless of whether the practice was misleading (at para.93):

> If it was only a question of whether there was a fair presentation of the financial position, the qualifying words "in accordance with GAAP" would serve no purpose. But, as the Handbook provides, GAAP is the standard against which fair presentation is to be judged. The opinion auditors give is that the financial position is, in accordance with accepted principles, fairly presented. It is, in that sense, a qualified opinion of fair presentation, and the qualification cannot be ignored.
>
> [emphasis in original]

64 It is my view that the aim of an auditor's report is to allow auditors to provide their professional opinion which may be relied upon as a guide to business planning and investment. GAAP may be their guide to forming this opinion, but auditors are retained to form an opinion on the fairness of the financial statements, not merely on their conformity to GAAP. A person to whom the auditor owes a duty of care who reads a standard auditor's report and concludes in reliance on it that the financial statements are fair is acting reasonably.

65 I find support for this view in Section 5400 of the Handbook. 5400.14 sets out the standard form of auditor's report. 5400.16 states, in part:

> To permit all auditors to judge in a consistent manner whether financial statements "present fairly", there must be a standard against which those judgments can be made; generally accepted accounting principles provide such a standard.

It is clear from the Handbook that the paramount aim in auditing and in providing an unqualified audit is to ensure that the financial statements "present fairly" the financial position of the company being audited. GAAP is a tool to achieve that fair presentation. But in my view auditors intend unqualified auditor's reports to mean that the financial statements present fairly the financial position. The tool used - GAAP - is intended to result in such fair presentation and when it does not the tool is revised, as it was in 1985 when it became clear that the practice of capitalizing unpaid interest could be misleading. Further, auditors, as professionals rendering their considered opinion, expect to induce reliance on that opinion - whether the reliance that they expect to induce is merely by company management or by a broad class of investors. Reliance is only reasonable if the unqualified auditor's report is taken to mean that the financial statements do present fairly the financial position of the company.

66 Given the aim in auditing, the understanding of audits that those who might rely on them have, and that auditors know of this understanding, auditors cannot hide behind the qualification to their reports ("according to GAAP")

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where the financial statements nevertheless misrepresent the financial position of the company. This does not open the floodgates to liability for auditors. The CICA has carefully drafted, and continues to improve and adapt with changing conditions, the Handbook and GAAP.

67 The defendant relies upon *Lapointe c. Hôpital Le Gardeur*, [1992] 1 S.C.R. 351 (S.C.C.) and *Sceptre Resources Ltd. v. Deloitte Haskins & Sells* (1991), 83 Alta. L.R. (2d) 157 (Alta. C.A.) as exemplifying the line of cases which hold that a professional defendant may avoid liability where the impugned conduct is in accordance with standard and approved professional practice.

68 The plaintiffs, on the other hand, referred us to what was said by McEachern C.J.S.C. (as he then was) in *Revelstoke Credit Union v. Miller*, [1984] 2 W.W.R. 297 at 303 (B.C. S.C.) and say that the standard of care should not be limited to GAAP. They submit that the standard of care as defined by law is to exercise such reasonable care as the circumstances require to ensure that representations made are accurate and not misleading. And, more specifically, that the defendant was required to exercise the care and skill which other competent auditors would have used in identical circumstances to ascertain whether the balance sheet truly exhibited the company's financial position according to the books and information obtained.

69 The present judicial attitude towards standards set by professions is set out by Sopinka J. for a majority of the Supreme Court of Canada in *ter Neuzen v. Korn* (1995), 11 B.C.L.R. (3d) 201 (S.C.C.) at para. 51:

> I conclude from the foregoing that, as a general rule, where a procedure involves difficult or uncertain questions of medical treatment or complex, scientific or highly technical matters that are beyond the ordinary experience and understanding of a judge or jury, it will not be open to find a standard medical practice negligent. On the other hand, as an exception to the general rule, if a standard practice fails to adopt obvious and reasonable precautions which are readily apparent to the ordinary finder of fact, then it is no excuse for a practitioner to claim that he or she was merely conforming to such a negligent common practice.

While this test does not allow a professional to be completely insulated from liability where a standard practice is followed, it is very deferential to standard practices: only "if a standard practice fails to adopt obvious and reasonable precautions which are readily apparent to the ordinary finder of fact" may the standard practice be held to fall below the standard of care. Auditors should state plainly their professional opinion that a set of financial statements present fairly the financial position of the company and have no fear that there will be an explosion of liability.

70 However, while deference will be shown to the professional standard, the court will not blindly accept it: a study of the authorities shows that selection of the appropriate standard of care is a question of law. In *Canadian National Railway v. Vincent*, [1979] 1 S.C.R. 364 (S.C.C.), Pratte J. said at 375:

> [I]t is up to the judge to lay down the criterion that will be used to determine whether there has been fault; this is undoubtedly a question of law. ...
>
> [T]he role of the jury is much broader, in my view, where the criterion that is to be used to determine whether there has been a quasi-delict is, as in the case at bar, the conduct of a prudent and reasonable man. In this case, while it is up to the judge to explain to the jury what is meant by this prudent and reasonable man whose behaviour is to be used as a criterion, it is up to the jury, on the other hand, to decide whether the conduct of the party being sued meets the requirements of this criterion.

See also *Wade v. Canadian National Railway*, [1978] 1 S.C.R. 1064 (S.C.C.)

71 This view is also evidenced by the text writers. In J. Fleming, *The Law of Torts*, 8th ed. (Sydney: The Law Book Company Limited, 1992) the learned author says at 106:

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> It is for the court to determine the existence of a duty relationship and to lay down in general terms the standard of care by which to measure the defendant's conduct; it is for the jury to translate the general into a particular standard suitable for the case in hand and to decide whether that standard has been attained ...

See also G.H.L. Fridman, Q.C., *The Law of Torts in Canada* (Toronto: Carswell, 1989) at 287; A.M. Dugdale and K.M. Stanton, *Professional Negligence*, 2nd ed. (London: Butterworths, 1989) at 235; and R.A. Percy, *Charlesworth and Percy on Negligence*, 8th ed. (London: Sweet & Maxwell, 1990) at 451.

72 This conclusion is also reached in *ter Neuzen* at para.52:

> The question as to whether the trier of fact can find that a standard practice is itself negligent is a question of law to be determined by the trial judge irrespective of the mode of trial.

73 In my view, therefore, while professional standards would normally be a persuasive guide as to what constitutes reasonable care, those standards cannot be taken to supplant or to replace the degree of care called for by law. A professional body cannot bind the rest of the community by the standard it sets for its members. Otherwise, all professions could immunize their members from claims of negligence. A partial immunization would be the result of giving effect to the "qualification" in unqualified auditor's reports that the financial statements present fairly the financial position "in accordance with GAAP". It is for this reason that I respectfully disagree with the learned trial judge that it is appropriate for auditors to sign unqualified auditor's reports if the financial statements are prepared in accordance with GAAP, if the auditors know or ought to know that the financial statements are misleading.

74 The issue therefore is whether it was a negligent misstatement for the defendant to say that the financial statements presented fairly the financial position of VMCL, giving all due deference to GAAP, the standard practice, as strong evidence of the appropriate standard of care, where the financial statements failed to disclose the amount of unpaid interest.

75 If it were not for the specific knowledge of the defendant in this case, the decision to give a standard auditor's report for financial statements that did not disclose the amount of unpaid interest would not have been one that fell below the applicable standard of care. Although from our present vantage point it appears that the amount of interest arrears should have been disclosed on the financial statements, and in fact GAAP was changed in 1985 to require such disclosure, it would be wrong to assume that an auditor who followed GAAP of the day was negligent. In *ter Neuzen*, Sopinka J. said (at para.34):

> It is also particularly important to emphasize, in the context of this case, that the conduct of physicians must be judged in the light of the knowledge that ought to have been reasonably possessed at the time of the alleged act of negligence. As Denning L.J. eloquently stated in *Roe v. Ministry of Health; Woolley v. Ministry of Health*, [1954] 2 All E.R. 131 (C.A.), at p.137, "we must not look at the 1947 accident with 1954 spectacles". That is, courts must not, with the benefit of hindsight, judge too harshly doctors who act in accordance with prevailing standards of professional knowledge. This point was also emphasized by this court in *Lapointe*, supra, at pp. 362-63:
>
> > ...courts should be careful not to rely upon the perfect vision afforded by hindsight. In order to evaluate a particular exercise of judgment fairly, the doctor's limited ability to foresee future events when determining a course of conduct must be borne in mind. Otherwise, the doctor will not be assessed according to the norms of the average doctor of reasonable ability in the same circumstances, but rather will be held accountable for mistakes that are apparent only after the fact.

76 It only became apparent during this period that GAAP needed to be changed, and when it did become clear, GAAP was changed. Until that time, GAAP held that unpaid interest was capitalized and reported as income. A note to that effect was provided in the financial statements, but the amount of arrears was not disclosed. This was, according to the evidence before the trial judge, the universal practice of financial companies like VMCL. It was the considered approach

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of Chartered Accountants as a profession, and thus a practice not to be lightly disturbed. The inappropriateness of this practice was because of the combination of a prolonged period of recession, making many debtors unable to service their mortgages, and the collapse in property values. In a generally rising market - as is the long-term norm - unpaid arrears will be fully secured and losses from them will be only a tiny fraction of the amount of the loans in default. In fact, to make a point of showing the potential liability for arrears would be misleading where the arrears were abundantly secured and there was no chance of loss.

77 However, Touche was not rendering its opinion after applying GAAP in a vacuum, i.e., without anything that would lead it to a belief that GAAP was insufficient or misleading. Touche had actual knowledge that a simple application of GAAP would omit material information and lead to financial statements that could not be said to have fairly presented the financial position of VMCL. Given this actual knowledge, Touche fell below the required standard of care when it made its auditor's report.

78 The trial judge discussed the state of knowledge of Touche's lead auditor, Mr. Brock, at paras. 24, 25, and 27:

> However, Mr. Brock did consider adding a note to the financial statements indicating the amount of mortgage loans in default. He proposed to the company that the amount be disclosed. His memorandum to the file indicates that he thought such "should allow the reader to better understand the possible risk inherent in an operation of this kind". He actually drew the form of note he had in mind:
>
> > Included in mortgages receivable are amounts of ______ where payments are in arrears. Management is of the opinion, that based on their past experience and the value of the underlying security, the company will realize full recovery.
>
> The amount he would have stated was never determined.
>
> Before the Auditors' Report was signed, Mr. Brock and one of his partners reviewed with Mr. Bessert [the principal of VMCL] what they considered the company's statements should disclose. They specifically discussed the loss provision in respect of loans where full recovery appeared questionable as well as the mortgages in arrears.
>
> .....
>
> Mr. Bessert firmly resisted noting the amount of loans in arrears. He took the position that it was not necessary. He told Mr. Brock he had obtained an opinion from another major accounting firm to the effect that the proposed disclosure was not a requirement of GAAP. Mr. Brock then researched the point. He concluded that the disclosure was not required for the statements to be in accordance with GAAP...

79 I agree with the learned trial judge's conclusion that Mr. Brock knew that this was material information. It was needed in the financial statements to present fairly the financial position of VMCL. The trial judge held at para. 79:

> In my view, it may be said at once that any question of whether this element of the company's financial position was material to the purchase of debentures is shortly put to rest on the evidence of Mr. Brock. It was apparent to him that the reason Mr. Bessert resisted the proposed disclosure was because it could impair the sale of debentures. It appears to me there can be no real question that what Mr. Brock knew would facilitate a better understanding of the risk was entirely material. It was because the information was material that its disclosure was resisted.

b. Was the acceptance of the deficient loss provision a breach of the standard of care?

80 Only with respect to the loss provision did the trial judge find the defendant negligent. The trial judge expressed his conclusion on this matter as follows, at para.120:

> Accepting that a loss provision is an estimate and that even considerable latitude, in both directions, is to be expected, it cannot be said that a stated income loss in the range of $300,000 instead of $92,000 would, clearly, not have been

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material to a purchaser; it may have affected his or her decision. In my view, that is sufficient to establish that the auditors fell below the standard of care required in conducting the audit of the '83 statements.

81 The defendant disagrees with the trial judge's conclusion that the understated loss provision was a material misrepresentation. The defendant says the conclusion is not only wrong, but is inconsistent with subsequent statements in the reasons for judgment. For example, the trial judge says at para.150:

> It cannot be said that a loss provision of a little greater than two percent of the assets and a $270,000 reduction in the $1.7 million cushion whereby assets exceeded liabilities would have caused the Kripps or the Thorpes to stop buying debentures after they received the '84 prospectus.
>
> (emphasis added)

And at para.157:

> In my view, there *may be a possibility, although it would seem remote, that the misstatement could have affected the decision of some who bought debentures* - it was a material misstatement - but it cannot be said that there is any basis on which it can properly be inferred that, had the loss provision been $394,500 instead of $125,000, the Kripps, the Thorpes or the Plunzs would have decided against the purchases that resulted in the ultimate loss of their money.
>
> (emphasis added)

82 The defendant says that the correct test of materiality is whether, on a balance of probabilities, the misrepresentation would have influenced a reasonable investor. It cites *L.K. Oil & Gas Ltd. v. Canalands Energy Corp.* (1989), 60 D.L.R. (4th) 490 at 496 (Alta. C.A.) . The defendant submits that the trial judge's conclusion as expressed in his para.157, quoted above, is a finding that a statement which may *possibly* have affected the investors' decision was material, and that this alone does not satisfy the correct test.

83 The plaintiffs say that the trial judge did not err in holding the understatement of the loss provision to be a material misrepresentation. The plaintiffs say that if the correct amount had been included in the operating statements of VMCL, it would have affected a number of matters. For example, it would have reduced the retained earnings from a positive $89,000 to a negative $125,000. It would have affected the borrowing capacity of VMCL, because the company had a borrowing policy limited to ten times equity. And it would have affected the interest coverage (the ratio of VMCL's interest income to interest payments), reducing it from 0.999 to 0.7646.

84 The plaintiffs say that the test of materiality is not whether from an objective point of view a reasonable individual would have been affected by the misstatement, but rather whether the statements were "capable of affecting the mind" of the reader. Relying on *Inland Kenworth Ltd. v. Commonwealth Insurance Co.* (1990), 48 B.C.L.R. (2d) 305 (B.C. C.A.) at 309, they say that the trial judge took the correct approach.

85 From these submissions it would appear that there are two or three different tests for materiality. The first test is whether a representation *might possibly* affect a decision; the second is whether a representation *is capable* of affecting a decision; and the third is whether a representation *would probably* affect a decision. I think that the first two tests are the same, and that the real distinction is between a representation that *might possibly* affect a decision and one that *would probably* affect a decision.

86 Even if the higher test of probability is the one properly to be applied, it seems to me that understatement of the loss provision by approximately $275,000 is material. It may be that the trial judge understated the test of materiality, but even if he had applied the correct test he ought to have concluded that the loss provision was a material misrepresentation because it would likely have had a significant effect on the plaintiffs' decision.

(4) Reliance

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87 The trial judge considered the issue of reliance only with respect to the loss provision. He held the view that the defendant was not responsible for any misrepresentation in respect of the $4.9 million worth of mortgages in arrears not disclosed in the financial statements, or the note concerning non-performing loans which was altered and moved from the financial statements to the body of the prospectus. He therefore made no finding as to whether the plaintiffs did or did not rely on the negligent misrepresentation in the auditor's report to the extent that it declared fair the financial statements that failed to disclose the amount of mortgage arrears.

88 Reliance is a question of fact. Where such a finding is based upon oral testimony, the assessment of witnesses, and decisions on credibility, it is a question which should be answered by a trial judge. Here, however, the trial judge heard no oral evidence but rather based his findings of fact on documents, on affidavit evidence, and on transcripts of cross-examination of various witnesses, including the plaintiffs. In these circumstances, and in the absence of any finding by the trial judge concerning reliance with respect to the misrepresentation about the mortgage arrears, it is open to this Court to make its own determination as to whether reasonable reliance has been proven. Moreover, it will be seen that, even with respect to the trial judge's finding of non-reliance by the plaintiffs on the loss provision, that conclusion is essentially a matter of inference from all of the circumstances. In my respectful view, this Court is in as good a position to draw, or to refuse to draw, the necessary inferences as was the trial judge.

89 It is to be remembered that there was an interlocutory appeal to this Court on the pleadings in which the Court affirmed the conclusions of the chambers judge that the only claims against the defendant which were not bound to fail were those "based on actual reliance by individual plaintiffs on the opinions of the accountants" (at para. 82) and that the plaintiffs' other claims of presumed or deemed reliance must be struck out.

90 It is useful to review the approach that the trial judge took. He held that reliance might be inferred in some circumstances, but where there was more than one possible inducement to the plaintiffs' conduct, the plaintiffs had the burden of proving that the misrepresentation relied upon was "fundamental" to their decision. He said at para.138:

> The burden of proving the inducement that constitutes actual reliance remains with the debenture holders throughout. If it can be inferred that they would not have purchased the debentures if the loss provision had been $270,000 greater, it is to be inferred from the evidence as a matter of fact, not as a matter of law. It is not for the auditors to prove the purchases would have been made in any event but rather for the debenture holders to prove they would not. That is what the debenture holders must do to discharge the burden they bear of establishing that the misstated financial position was, in conjunction with other factors, fundamental to their decisions.

91 And at paras. 141 & 143:

> For the debenture holders to say they would not have purchased any debentures if they had known the financial statements were not correct is not the same as saying they would not have decided to make the purchases they did if they had known the true financial position. What they say does not address the question that must be answered: whether they were each induced by the extent to which the financial position was misstated. Their statement side-steps what is at issue; it is not related to any considered error or errors in the financial statements; it is not meaningful.
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> . . . . .
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> Actual reliance may, without more, be inferred where only the impugned representation and nothing else could have induced the decision taken by a plaintiff to enter the transaction which led to the loss, but that is not suggested here. Further, particularly in respect of financial statements, I consider the gravity of a misrepresentation may be so great that it is obvious, beyond question, that the plaintiff would not have entered into the transaction had the financial position been correctly presented. But that cannot be said here either.

92 The trial judge reviewed the evidence, including the plaintiffs' evidence with respect to the loss provision and the extent to which it might have induced the plaintiffs to invest, and he said at paras.153-4:

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> In my view, the Kripps and the Thorpes were induced to make the purchases that led to their losses by the experience they had enjoyed over many months of earning a very competitive rate of interest on their capital which they appear to have regarded as entirely secure. The level of confidence they say they had in late 1984 and early 1985 was, as it turned out, far from justified, but in any event, it was a product of the reliance they placed on the company's representations, not on the Auditors' Report and the '83 financial statements. I accept that when they first bought debentures in early 1983 they reviewed the company's financial statements with some care, but I do not consider their review in the fall of 1984 was fundamental to their purchase of debentures then, at least not to the extent that a greater loss provision would have made any difference to them.
>
> The Plunzs are in no materially different position than the Kripps and the Thorpes. When the prospectus was delayed in the spring of 1984, they did take their money out of VMCL. They never saw the quarterly report. They waited until they had received and reviewed the prospectus before purchasing more debentures. But apart from that and Mr. Plunz having been able to make a more knowledgeable review of the '83 statements, their position is no different and, it appears to me, they too have fallen short of establishing they would not have made the purchases they did in 1985 if the loss provision had been $270,000 greater than it was.

93 He stated his conclusions on reliance as follows, at para.157:

> I find that neither the Kripps nor the Thorpes nor the Plunzs were induced to purchase VMCL debentures after receiving its '84 prospectus by the extent to which the financial position of the company was misstated as a result of the loss provision having been inadequate. In my view, there may be a possibility, although it would seem remote, that the misstatement could have affected the decision of some who bought debentures - it was a material misstatement - but it cannot be said that there is any basis on which it can properly be inferred that, had the loss provision been $394,500 instead of $125,000, the Kripps, the Thorpes, or the Plunzs would have decided against the purchases that resulted in the ultimate loss of their money. They have not discharged the burden of proof they bear.

94 With respect, it is my view that the learned trial judge made two errors in reaching this conclusion: First, he treated the misstatement for which the defendant is liable as the misstated loss provision in the financial statements. However, and acknowledging that the defendant also breached its duty of care in dealing with the mortgage arrears, the defendant's misstatement is the auditor's report that the financial statements presented the financial position of VMCL fairly. Second, he misstated the test and set too high a standard for the plaintiffs to meet.

95 On the question of the statement to which the test should be applied, the plaintiffs were not owed a duty of care that the audit be carried out properly; they were owed an auditor's report that could reasonably be relied upon. The defendant's negligent misstatement was the unqualified auditor's report. It did not make the financial statements. While they may have had significant input into - or even prepared - the financial statements, those statements were signed by the company and purported to be statements of the company. If the defendant owes any duty for the preparation of the financial statements it is to the company; *vis-à-vis* third parties, it can only be liable for the auditor's report. The issue therefore is whether the plaintiffs would have invested had the prospectus they read contained a qualified audit.

96 On the question of the appropriate test, the plaintiffs say a representation is material when its natural tendency or probable effect is to induce a representee to act upon it as reliable. The plaintiffs say that when a material misrepresentation is acted upon by the representee, there is an inference of an inducement to act in reliance upon the misrepresentation. That inference arises unless the representor shows that the representee had knowledge of the true facts, or the representee's conduct shows that there was not reliance on the representation. The plaintiffs say that it is sufficient for them to prove that the misrepresentation sued upon was one of several material factors inducing the decision to invest. They say they need not show that the misrepresentation was the sole, or even the fundamental, factor causing them to act as they did. In support of this proposition, the plaintiffs cite *Parallels Restaurant Ltd. v. Yeung's Enterprises Ltd.* (1990), 4 C.C.L.T. (2d) 59 (B.C. C.A.); *Redgrave v. Hurd* (1881), 20 Ch. D. 1 (Eng. C.A.); *Arnison v. Smith* (1889), 41 Ch. D. 348 (Eng. C.A.), at 369; *Bell v. Buschlen/Mowatt Fine Art Investments Ltd.* (1988), 32 B.C.L.R.

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(2d) 349 (B.C. C.A.) at 374; *Australian Steel & Mining Corp. Pty. Ltd. v. Corein*, [1974] 2 N.S.W.L.R. 202 (New South Wales C.A.) at 207; *Power v. Kenny*, [1960] W.A.R. 57 (Australia S.C.); and *Sidhu Estate v. Bains* (1996), 25 B.C.L.R. (3d) 41 (B.C. C.A.).

97 The defendant says that the plaintiffs' argument amounts to an assertion that a finding of material misrepresentation is tantamount to a finding of reliance. It says that although reliance may be inferred in some circumstances, it is an issue of fact. The inference is one which may be drawn, in the absence of direct evidence, but it is not an inference that must be drawn. The defendant says there is nothing in the circumstances of this case which would compel a finding of reliance. In fact, there was evidence, the defendant says, that what induced the plaintiffs to buy VMCL's debentures were the favourable interest rates offered, and that if the plaintiffs had seen a loss provision in the financial statement of $394,500 it would not have affected their investment decisions. It says this evidence supports the trial judge's finding of no reliance, a finding which should not be interfered with by this Court.

98 This Court recently held in *Sidhu Estate v. Bains, supra*, an action in deceit, that liability may be found where the plaintiff's reliance on a fraudulent misrepresentation is only one of several factors inducing her to act. And it held, relying on *Parallels Restaurant, supra*, that where a defendant has made a material misrepresentation calculated to induce the plaintiff to act as she did, and where the loss is consistent with the plaintiff having acted on the misrepresentation alleged, the burden of proof shifts to the defendant to prove that the plaintiff did not rely at all on that misrepresentation. Anderson J.A. giving the judgment of the Court in *Parallels Restaurant* said at 68:

> In my opinion, once the plaintiff has proved a false representation of a material fact, the evidentiary burden shifts to the defendant to clearly show that the plaintiff was not induced by the false representation.

99 To the same effect are *Power v. Kenny, supra*, another case of fraudulent misrepresentation, *per* Wolff C.J. at 63-4 and Virtue J., in a concurring judgment at 65-6; *Arnison v. Smith, supra*, another action in deceit, *per* Lord Halsbury L.C. at 369 (cited with approval in *Bell v. Tinmouth, supra*); and *Australian Steel & Mining Corp., supra.*

100 The defendant sought to distinguish these authorities on the basis that they were all cases where fraud was alleged and that no such rule or principle is to be found in cases where the claim is based on negligent misrepresentation. The defendant says that in cases of negligent misrepresentation, the burden of proving reliance never shifts to the defendant.

101 I am not persuaded that there is any merit in this distinction. Whether a representation was made negligently or fraudulently, reliance upon that representation is an issue of fact as to the representee's state of mind. There are cases where the representee may be able to give direct evidence as to what, in fact, induced him to act as he did. Where such evidence is available, its weight is a question for the trier of fact. In many such cases, however, as the authorities point out, it would be unreasonable to expect such evidence to be given, and if it were it might well be suspect as self-serving. This is such a case.

102 The distinction between cases of negligent and fraudulent misrepresentation is that proof of a dishonest or fraudulent frame of mind on the defendant's part is required in actions of deceit. That, too, is an issue of fact and one which may also, of necessity, fall to be resolved by way of inference. There is, however, nothing in that which touches on the issue of the plaintiff's reliance. I can see no reason why the burden of proving reliance by the plaintiff, and the drawing of inferences with respect to the plaintiff's state of mind, should be any different in cases of negligent misrepresentation than it is in cases of fraud.

103 It is sufficient, therefore, for the plaintiff in an action for negligent misrepresentation to prove that the misrepresentation was at least one factor which induced the plaintiff to act to his or her detriment. I am also of the view that where the misrepresentation in question is one which was calculated or which would naturally tend to induce the plaintiff to act upon it, the plaintiff's reliance may be inferred. The inference of reliance is one which may be rebutted but the onus of doing so rests on the representor.

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104 Applying the principles derived from the cases referred to above, in my respectful view, the learned trial judge misdirected himself on the law in holding that to succeed the plaintiffs had to prove that the misrepresentation alleged to be relied upon was "fundamental" to their decision, and in holding that affirmative evidence from the plaintiffs was required before actual reliance could be found. In my respectful view, the misrepresentation with respect to the understated loss provision was material, and, because of its effect on retained earnings, borrowing capacity, and interest coverage, was such as would tend to induce the plaintiffs to act in reliance upon it.

105 Moreover, the non-disclosure of $4.9 million worth of mortgages in arrears and the misrepresentation with respect to the non-performing loans note were decidedly material and misleading. They were misrepresentations in financial statements which the defendant said fairly represented the financial picture of VMCL. They were statements which clearly would tend to induce an investor to purchase VMCL debentures. It was therefore incumbent upon the defendant to rebut the inference that the plaintiffs relied on these misrepresentations, and in my view it failed to do so.

(5) Damages

106 The fifth element required in a negligent misrepresentation claim - that the reliance result in damages - is not at issue on this appeal.

V Conclusion

107 I conclude that the plaintiffs have made out a successful claim for negligent misrepresentation. The defendant owed the plaintiffs a duty of care, a material misrepresentation was negligently made, and the plaintiffs relied upon this misrepresentation to their detriment.

108 I would allow the plaintiffs' appeal.

***Ryan J.A.* (dissenting):**

109 I am unable to agree with my colleague Mr. Justice Finch that this appeal must be allowed.

110 I will not repeat the facts as Mr. Justice Finch has thoroughly canvassed them in his reasons for judgment.

111 The appellants appeal the decision of the trial judge on the basis that he erred in:

> 1. failing to hold that Touche made a negligent misrepresentation by failing to provide full disclosure of the $4.9 million of mortgage loans in default when Touche knew that the purpose of the audit of the financial statements was to market debentures and that readers of the financial statements would be relying on the document for the purpose of their investment decision;
>
> 2. finding that the plaintiffs had not relied on the audited financial statements.

Were The Financial Statements Misleading?

112 At the time in question the *Securities Act*, R.S.B.C. 1979, c. 380, compelled Victoria Mortgage Corporation Ltd. to file a prospectus with the Superintendent of Brokers. The *Securities Act* required that the prospectus contain the financial statements of the company as well as an auditor's report. The relevant portion of s. 42 of the Act provided:

> 42. (1) *A prospectus shall, except as otherwise provided in this Act, contain a report on the financial statements contained in it of a person* acceptable to the superintendent *who is the auditor of the company* or of a subsidiary or is an accountant eligible for appointment as auditor of the company or of a subsidiary and, where financial statements of a business acquired or to be acquired are required or permitted, a report of a person acceptable to the superintendent who is the auditor of the business or is an accountant eligible for appointment as the auditor, *which report shall be signed by the appropriate auditor* or accountant *and shall state whether in the opinion of the auditor or accountant the*

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> *financial statements referred to in it present fairly the financial position of the company*, the subsidiary, or the business acquired or to be acquired, as the case may be, *and the results of their respective operations for the years and periods under review in accordance with generally accepted accounting principles applied on a consistent basis.*
>
> [emphasis added]

113 Touche was engaged by Victoria Mortgage Corporation Ltd. to provide the auditors' report. Touche audited the company's financial statements and issued a standard form of auditors' report prescribed by the Canadian Institute of Chartered Accountants. The report was also in conformity with the requirements of s. 42(1) of the *Securities Act*. The report read:

> We have examined the balance sheet of Victoria Mortgage Corporation Ltd. as at December 31, 1983 and 1982 and the statements of operations and retained earnings and changes in financial position for the year then ended; and the consolidated statements of operations, retained earnings and changes in financial position of the year ended December 31, 1981, the four months ended December 31, 1980 and the year ended August 31, 1980. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.
>
> *In our opinion, these financial statements present fairly the financial position of the Company as at December 31, 1983 and 1982, and the results of its operations and the changes in its financial position of the years ended December 31, 1983, 1982, and 1981, the four month period ended December 31, 1980 and the year ended August 31, 1980 in accordance with generally accepted accounting principles applied on a consistent basis.*
>
> [emphasis added]

114 The financial statements and auditors' report were included in the 1984 prospectus issued by Victoria Mortgage Corporation Ltd. in accordance with the requirements of the *Securities Act*.

115 It was common ground at trial that as at December 31, 1983 one-third of the company's loans were in default 90 days or more. The company's financial statements did not differentiate between accrued interest on up-to-date loans or those in default. The financial statements recorded accrued interest from both as income under the heading "mortgages receivable". Nowhere in the financial statements was it noted that a significant number of loans were in default. The appellants contended that the total amount of all interest unpaid but capitalized ($729,000) ought to have been disclosed either in the Statement of Changes in Financial Position or in a further note. Without such disclosure the appellants say that the financial position of the company was inaccurately portrayed. It was the appellants' position that the auditors were negligent in stating that "the financial statements present fairly the financial position of the company".

116 In showing accrued interest on default loans as income in this way the company was following its stated policy as described in the "notes to the financial statements". In the notes the company stated its accounting policy with respect to mortgages receivable to be this:

> The Company's policy on mortgages in default is to capitalize accrued interest and legal fees to the book value of the mortgage if, in management's opinion, these amounts are adequately secured. Where the Company holds title to property as a result of foreclosure proceedings, the book value of the mortgage is transferred to real estate investments and the property is held until such time that the book value of the mortgage is recoverable.

117 The trial judge analyzed the method of reporting accrued interest and discussed whether the default loans should have been disclosed in the way contended for by the appellants. He said (at paras. 80-2):

> It is, however, important to emphasize at the outset that the company's policy with respect to capitalizing interest was clearly stated in the notes to the financial statements and that it was a policy that was entirely appropriate for a lending institution or mortgage company. It was well recognized to be consistent with generally accepted principles

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of accounting. Indeed, an early draft of Mr. Roberts' report reveals that he considered any criticism of VMCL's policy "untenable".

GAAP is discussed, if not defined, in the Handbook (1000. 59-60):

> Generally accepted accounting principles is the term used to describe the basis on which financial statements are normally prepared...
>
> [It] encompasses not only specific rules, practices and procedures relating to particular circumstances but also broad principles and conventions of general application, including the underlying concepts described in this Section. Specifically, [GAAP] comprise[s] the Accounting Recommendations in the Handbook and, when a matter is not covered by a Recommendation, other accounting principles that either:
>
> > (a) are generally accepted by virtue of their use in similar circumstances by a significant number of entities in Canada; or
> >
> > (b) are consistent with the Recommendations in the Handbook and are developed through the exercise of professional judgment...

In terms of auditing standards the Handbook (5400.16) provides:

> To permit all auditors to judge in a consistent manner whether financial statements "present fairly", there must be a standard against which those judgments can be made; generally accepted accounting principles provide that standard...

In 1984, the effect of the application of the policy was that unpaid interest, considered by a company's management to be adequately secured, was treated as income and stated to be revenue. Because it was capitalized, it was also added to the loan balances thereby increasing stated assets. If it was considered not to be secured, a loss provision was to be made but, apart from any loss provision, financial statements prepared on this basis disclosed neither the amount of capitalized interest nor the amount of loans in default. It was not generally accepted as an accounting principle that they should do so. The several audited financial statements of various banks and lending institutions from 1983 that are in evidence make this quite clear; it was not GAAP -- not the basis on which financial statements were normally prepared.

118 As Mr. Justice Finch has noted the trial judge found that the loss provision which Touche required - $125,000 - was inadequate. But the first question the trial judge had to answer was whether the amount of the loans in default was so large as to have been clearly material to users of the financial statements that there ought to have been a note to the financial statements setting out the amount of the interest or the amount of the loans in default. He concluded that it was not required. In analyzing the question the trial judge made a number of important points and findings:

> [T]he function of an auditor must be kept in mind. The preparation of draft financial statements in the form considered appropriate is customarily done during the course of an audit. But the statements on which auditors report are the company's statements, not the auditors'. They are engaged to express an opinion on the company's presentation of its financial position. [para. 85]
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> .....
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> If it was only a question of whether there was a fair presentation of the financial position, the qualifying words "in accordance with GAAP" would serve no purpose. But, as the Handbook provides, GAAP is *the* standard against which fair presentation is to be judged. The opinion auditors give is that the financial position is, in accordance with accepted principles, fairly presented. It is, in that sense, a qualified opinion of fair presentation, and the qualification cannot be ignored. [para. 93]
>
> .....

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> I do not consider there to be a sound evidentiary basis on which it could be fairly concluded that it is a generally accepted accounting principle that everything of a financial nature that is material must be disclosed on financial statements. That assertion is not to be found in *any* of the experts' reports and it certainly cannot be taken from what is quoted from the Handbook. What the experts do say is that it is implicit in a fair presentation that the financial position not be materially misstated. [para. 87]
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> Compliance with a standard may be a matter of judgment, but to be meaningful, the standard against which a presentation is made must be largely objective. I much prefer the more cogent evidence of Mr. Selman and Mr. Yule [expert witnesses called by the defendant] who both say that, in 1984, there was simply no accepted principle whereby the amount of loans that were not current and the amount of capitalized interest ought to have been stated in the '83 financial statements of VMCL. Under cross-examination Mr. Selman says GAAP does not require everything that is material to be stated. He explains that the consideration of any item in a financial statement is a two-step process. First one decides whether, as a matter of the prevailing practice in the profession (GAAP), disclosure is to be made. If so, then one decides if the item is material. But if the item is not one that accepted practice dictates be disclosed, the question of materiality does not arise. It is not generally accepted that everything of a financial nature that may be of interest to the user of a financial statement -- everything that is material -- must be stated. That is not the standard against which the fair presentation of the financial position must be judged. That is not GAAP. [para. 94]
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> . . . . .
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> I find that the auditors rightly decided that, particularly in the absence of any question about the viability of the company as a going concern, there was at the time no generally accepted accounting principle whereby the amount of loans that were not current and the amount of capitalized interest were to be stated in the '83 financial statements despite the relatively large amounts involved. [para. 96]

119 The trial judge next considered whether, knowing that the financial statements were to be included in a prospectus, the auditors bore a "higher obligation" such that they should have insisted on disclosure or refused to sign. The trial judge found that it was implicit in the auditors' terms of engagement that if the statements fairly presented the financial position in accordance with GAAP, the report the company required to carry on its business would be given. He said (at para. 100):

> I do not accept that there was some higher obligation assumed by the auditors in the sense that it was incumbent on them to insist on disclosure regardless of GAAP because they knew that the particular purpose of the statements audited was to facilitate the sale of debentures to the public. The auditors were not engaged to prepare a financial presentation to prospective purchasers; they were engaged to conduct an audit and give the standard form of report. Their function was not to develop some kind of a financial risk evaluation; it was only to determine and report on whether the company's statements were as they should be, having regard for the accepted principles by which accountants were then guided. They were entitled to accept the engagement, conduct the audit, and give their report assuming that it would be relied upon by those who reasonably understood the meaning of the company's stated accounting policies and the stated standard against which the fairness of the presentation was judged. It simply cannot be said that, in terms of disclosure, the auditors were required to adopt some different standard than that which they stated and which they were engaged to apply.

120 The appellants attack the finding of fact by the trial judge that the generally accepted accounting principles did not require the disclosure of the amount of loans in default. The trial judge was asked to choose between competing experts. The appellants have pointed to nothing in the evidence which demonstrates that the trial judge was clearly wrong in choosing as he did or that his findings were unreasonable. I have set out the findings of the trial judge. I do not find it necessary to repeat the lengthy evidence upon which he made his decision. I would not give effect to this aspect of the appellants' appeal.

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121 Next the appellants submit that the trial judge erred in failing to hold the respondent to a higher standard in preparing their audit report. Their submission is that given the use to which the auditors knew that the financial statements would be used they ought to have insisted on disclosure of material that would assist a prospective buyer in making his or her decision. In my view the trial judge was correct in holding that the auditors were retained to perform a standard audit with respect to the financial statements. I agree with his conclusion that it simply cannot be said that the auditors were required to adopt some different standard than that which they stated they were engaged to apply.

122 Put simply, the *Securities Act*, and the auditors' retainer, required the auditors to answer this question: Do the financial statements reveal the company's financial position in accordance with the standard by which such statements are measured? The auditors correctly identified the standard by which the statements were to be measured and gave their opinion that the financial statements met that standard. That is all they were asked to do. They cannot be said to be negligent on that basis, nor can they be said to be negligent by failing to answer a question they were not asked. It is true that the auditors were aware that the financial statements would be included in prospectuses that prospective purchasers would examine. But, as the trial judge pointed out, prospective purchasers would know by an examination of s. 42 of the *Securities Act*, and the auditors' report itself, "the stated standard by which the fairness of the presentation was judged". The auditors owed no duty to prospective purchasers to go beyond what was required by their terms of engagement.

123 In the case at bar my colleague has found that the generally accepted accounting principles were themselves inadequate. In my respectful view that finding does not assist the appellants. The respondents were asked to determine the prevailing principles (GAAP) and state whether the financial statements met them. They did that. They are not accused of negligently determining the proper generally accepted accounting principles, they are accused of failing to state that the prevailing principles were inadequate. In my view they were under no obligation to offer such an opinion.

The Reliance Issue

124 The trial judge found that the financial statements were misleading in that they provided an inadequate loss provision with respect to the loans in default. The trial judge found however that the financial statements did not induce the appellants to purchase the debentures. His essential findings were these:

> [T]he Kripps and the Thorpes were induced to make the purchases that led to their losses by the experience they had enjoyed over many months of earning a very competitive rate of interest on their capital which they appear to have regarded as entirely secure. The level of confidence they say they had in late 1984 and early 1985 was, as it turned out, far from justified, but in any event, it was a product of the reliance they placed on the company's representations, not on the Auditors' Report and the '83 financial statements. I accept that when they first bought debentures in early 1983 they reviewed the company's financial statements with some care, but I do not consider their review in the fall of 1984 was fundamental to their purchase of debentures then, at least not to the extent that a greater loss provision would have made any difference to them. [para. 153]
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> . . . . .
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> I consider that the Plunzes were induced to buy the debentures by the attractive rate of interest they could earn in what they perceived to be an absence of any real risk to their capital. Like that of the Kripps and the Thorpes, their confidence, which proved to be ill-founded, was derived from the representations made by VMCL in the prospectus, not by the auditors. The evidence does not establish that the extent to which the financial position in December '83 was misstated was fundamental to the purchases they made more than a year later.
>
> **Conclusion**
>
> I find that neither the Kripps nor the Thorpes nor the Plunzes were induced to purchase VMCL debentures after receiving its '84 prospectus by the extent to which the financial position of the company was misstated as a result of the loss provision having been inadequate. In my view, there may be a possibility, although it would seem remote, that the misstatement could have affected the decision of some who bought debentures -- it was a material

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> misstatement -- but it cannot be said that there is any basis on which it can properly be inferred that, had the loss provision been $394,500 instead of $125,000 the Kripps, the Thorpes, or the Plunzes would have decided against the purchases that resulted in the ultimate loss of their money. They have not discharged the burden of proof they bear. [paras. 156-7]

125 It is clear from these passages that the trial judge did not dismiss the appellants' case on the basis that they had failed to discharge the burden of proof as it related to reliance, he made a clear finding that the appellants were induced by high interest rates and representations by the company to purchase the debentures. I am not persuaded that these findings are unjustified. For that reason I would dismiss the appeal.

126 In any event I am not persuaded that the trial judge erred in law in determining that the burden of proof lay with the appellants to prove on a balance of probabilities that they had relied on the misrepresentations in purchasing their debentures. In my view the trial judge correctly analyzed the issue in the following passage from his reasons for judgment (at paras. 137-8):

> *L.K. Oil & Gas Ltd. v. Canalands Energy Corp.* (1989), 60 D.L.R. (4th) 490, was a case in which the Alberta Court of Appeal considered whether a material misrepresentation in the estimate of profitability induced the plaintiff to purchase certain oil and gas interests. There it was contended that, where a material misrepresentation is made with the intention that it induce a person to enter into a contract an inference is to be drawn that the person was induced to make the contract. The court rejected the contention citing authority for the proposition that, while the inducement may be a fair inference of fact, it cannot be an inference of law: *Smith v. Chadwick* (1884), 9 App. Cas. 187 (H.L.). The court concluded (p. 498):
>
>> In my view, the approach taken by Canadian courts is to consider all of the relevant facts of a case in order to decide whether a statement was relied upon. Where nothing else but the representation could have induced the contract, then a logical inference is that the representation did, in fact, induce the contract. Where other factors could be operative, the evidence must be considered to determine which factors were called upon. Lord Blackburn noted in *Smith v. Chadwick*, the weight of the inference as evidence must "greatly depend upon the degree to which the action of the plaintiff was likely, and on the absence of all other grounds on which the plaintiff might act".
>
> I consider this to be the principle that must govern the determination of liability in this case. The burden of proving the inducement that constitutes actual reliance remains with the debenture holders throughout.

127 The appellants relied upon cases dealing with fraud for the proposition that the burden of proof on the issue of reliance is reversed once the misrepresentation is proved. Mr. Justice Finch has reviewed these cases. I find the fraud cases, which involve an element of deceit, of little assistance in the resolution of this issue. In my view the law in this area is settled and was correctly stated by the trial judge in the passage I have reproduced above quoting from the Alberta Court of Appeal in *L.K. Oil & Gas Ltd. v. Canalands Energy Corp.* (1989), 60 D.L.R. (4th) 490 (Alta. C.A.) . I see no compelling reason to change it.

128 Mr. Justice Finch has discussed and rejected the respondent's submissions supporting the trial judgement on an alternative basis. Since I am of the view that the appellants' grounds of appeal cannot succeed I need not deal with the respondent's other arguments.

Conclusion

129 I would dismiss the appeal.

Appeal allowed.

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End of Document

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TAB 10

2016 BCCA 471
British Columbia Court of Appeal

Soprema Inc. v. Wolrige Mahon LLP

2016 CarswellBC 3278, 2016 BCCA 471, [2017] 4 W.W.R. 87, [2017] B.C.W.L.D. 14, [2017] B.C.W.L.D. 43, 273 A.C.W.S. (3d) 281, 405 D.L.R. (4th) 594, 90 B.C.L.R. (5th) 318, 93 C.P.C. (7th) 60

Soprema Inc., Conax Properties Ltd. and Crigel S.A. (Appellants / Plaintiffs) and Wolrige Mahon LLP (Respondent / Defendant) and Ali Nanji and Amelia Holdings Group Limited (Respondents)

Groberman, Harris, Fenlon JJ.A.

Heard: October 4, 2016
Judgment: November 28, 2016
Docket: Vancouver CA43674

Proceedings: reversing *Soprema Inc. v. Wolrige Mahon LLP* (2016), [2016] B.C.J. No. 937, 2016 BCSC 813, 2016 CarswellBC 1260, Grauer J. (B.C. S.C.); additional reasons at *Soprema Inc. v. Wolrige Mahon LLP* (2016), 2016 BCSC 1184, 2016 CarswellBC 1775, Grauer J. (B.C. S.C.)

Counsel: S. Batkin, P. Waldkirch, for Appellants, Soprema Inc., Conax Properties Ltd. and Crigel S.A.
H. Mickelson, Q.C., L. Kotler, for Respondent, Wolrige Mahon LLP
J.K. McEwan, Q.C., T. Bant, for Respondents, Ali Nanji and Amelia Holdings Group Limited

Subject: Civil Practice and Procedure

APPEAL by plaintiffs from judgment reported at *Soprema Inc. v. Wolrige Mahon LLP* (2016), 2016 BCSC 813, 2016 CarswellBC 1260, [2016] B.C.J. No. 937 (B.C. S.C.) ordering disclosure of documents.

Harris J.A.:

Introduction

1 The issue on this appeal involves the test for determining when a party has impliedly waived solicitor-client privilege in the course of litigation by making its state of mind a material issue. More specifically, it engages the question whether and how the implied waiver, in such a situation, requires the party to have made its understanding of its legal position relevant or material by voluntarily putting that understanding in issue in litigation.

2 The issue arises in a negligent misrepresentation case. To succeed, the plaintiff must prove that it relied in fact and relied reasonably on an alleged misrepresentation. Accordingly, its "state of mind" is in issue. It appears the plaintiff received legal advice about the transaction, but it does not rely on that advice to demonstrate that it reasonably relied on the misrepresentation. It has not, in this sense, *voluntarily* made its understanding of its legal position a material issue in the litigation. Nonetheless, the legal advice it received may be relevant to its "state of mind" because it bears on the question whether the reliance was reasonable. In this judgment I will refer to a party *voluntarily* putting its legal understanding in issue to reflect this distinction.

3 The judge concluded that the test for waiver is not limited to circumstances where a party has voluntarily put its understanding of its legal position in issue. He concluded that a party may impliedly waive privilege if it put its "state of mind" in issue in a manner establishing a clear nexus between its state of mind and the privileged communications.

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Where the privileged communications may be "highly relevant" to the state of mind, fairness and consistency may require waiver if upholding the privilege would confer an "unfair litigation advantage" on the party claiming the privilege. The decision whether privilege has been waived involves the court in a "gatekeeper" function, assessing the specific facts to balance the interest in maintaining privilege against fairness and consistency in litigation.

4 For the reasons that follow, I would allow the appeal.

Background and Reasons for Judgment

5 The issue arose in an action alleging negligent misrepresentation against an auditor. Soprema, by which I mean the plaintiffs and appellants (in CA43674) here, alleges that Wolrige, the auditor, made false representations concerning the accuracy of certain financial statements on which it relied in deciding whether to exercise an option to purchase certain shares. Soprema alleges that it expected those financial statements to be used in the valuation of the fair market value of the shares. Wolrige denies both that Soprema relied on its representations and that any reliance was reasonable.

6 It is common ground that Soprema has not pleaded that it relied on Wolrige for legal advice or that information provided by Wolrige has affected its understanding of its legal position. Moreover, it has not pleaded that it relied on Wolrige's representations as a result of legal advice. It has not voluntarily made its understanding of its legal position a material issue in the litigation, in these kinds of ways. I reiterate that when I refer to voluntarily putting legal advice in issue, I am capturing this idea. On the other hand, Soprema received legal advice during the material period about the subject transaction. Its "state of mind" is a relevant issue in the litigation because to make out the cause of action it must have relied reasonably on the alleged misrepresentation and its understanding of its legal position is, arguably, relevant to whether its reliance was reasonable. Having said that, Soprema does not seek to justify the reasonableness of its reliance on the basis that it acted on legal advice. Nor has it sought to rely on legal advice or its understanding of its legal position in the discovery process.

7 Soprema produced a List of Documents claiming solicitor-client privilege over numerous documents. Wolrige applied for disclosure of approximately 250 documents which had been generated during a crucial period when Soprema alleged it relied on Wolrige's representations. The application focused on documents generated between May 28 and July 13, 2012. The period begins just before the date of the alleged representations and ends just after the date on which Soprema exercised the options.

8 The claim of privilege was supported by an affidavit from Soprema's in-house counsel, Mr. Belisle. It, and the descriptions on the List of Documents, disclosed that the documents related to a number of matters. These were summarized by the judge:

> [90] Mr. Belisle goes on to describe the documents in question. The first subset comprises "communications with outside counsel". Some of these do not list any outside counsel as author or recipient but are either authored by Mr. Belisle or were received by him, while approximately nine others showed no involvement of either Mr. Belisle or outside counsel.
>
> [91] Mr. Belisle deposes that these were (1) communications made for the purpose of requesting or receiving confidential legal advice for Soprema, or providing information to be used by external counsel in providing confidential legal advice to Soprema, or (2) communications between Soprema and/or Mallette personnel forwarding and/or discussing confidential legal advice received or to be sought from the external counsel. He then set out a number of legal issues, one or more of which, he deposed, were addressed by these communications.
>
> [92] The second subset comprises "in-house counsel documents". These mostly consist of communications involving Mr. Belisle, but some do not show him as either offering [authoring] or receiving them. Mr. Belisle deposes that these were (1) communications between personnel at Soprema and/or Mallette and Mr. Belisle for the purpose of requesting or receiving confidential legal advice for Soprema, or for providing information to be used by Mr. Belisle in providing confidential legal advice to Soprema, (2) confidential communications between Soprema and/

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> or Mallette forwarding and/or discussing confidential legal advice received from Mr. Belisle, or (3) confidential communications with others for the purpose of obtaining confidential appraisal information for the purpose of legal advice being provided by Mr. Belisle to Soprema. Once again, Mr. Belisle sets out the "legal issues affecting Soprema" with respect to which he provided such confidential legal advice. These include "potential claims against . . . Wolrige, and others".
>
> [93] The third subset consists of 30 documents grouped under the heading "internal privileged documents" which were neither authored nor received by legal counsel. According to Mr. Belisle, these consist of confidential communications (1) between personnel within Soprema and/or Mallette made for the purpose of identifying or discussing information to be provided to legal counsel so that it could be incorporated into legal advice to be provided to Soprema, and discussing legal advice that had been provided to Soprema; and (2) between Soprema and/or Mallette personnel and a real estate appraiser instructing and obtaining confidential information from him for the purpose of confidential legal advice being provided to Soprema.
>
> [94] An outline of the legal issues addressed in these documents is again provided, and include the financial affairs of the Convoy Group; valuation of the Convoy Group's properties; the reserves improperly kept by the Convoy Group; overcharging of Soprema by the Convoy Group; and the valuation of the shares of the Convoy Group.

9 Mallette is a confidential advisor to Soprema. It is subject to an express contractual duty of confidentiality. It was authorized by Soprema to request and receive legal advice from Mr. Belisle or outside counsel. Privilege over those communications was maintained on the basis that they were generated for the purpose of being provided to Soprema's legal advisors. As the judge expressed it at para. 89: "In this way, Soprema argues, Mallette would be either a 'conduit' for the passing of advice between solicitor and client, or an 'interpreter' for the benefit of counsel. Such claims to solicitor-client privilege over third-party communications are discussed very helpfully by Doherty J.A. in *General Accident Assurance Co. v. Chrusz* (1999), 180 D.L.R. (4th) 241 (Ont. C.A.) at 276-279."

10 The judge undertook a detailed analysis of the claimed privilege. With certain limited exceptions, he concluded that the claim to privilege had been established. He requested certain documents be provided to him for examination. This occurred. He upheld the claim in respect of some, but not all of the documents. The foundation of his conclusion upholding privilege is found at paras. 96-98:

> [96] In asserting privilege, Soprema relies upon the third party communications and "continuum of communications" principles discussed [in] the *General Accident* case and in cases such as *Camp Development Corporation v South Coast Greater Vancouver Transportation Authority*, 2011 BCSC 88 at paras 40-44. In *Descôteaux v Mierzwinski*, [1982] 1 SCR 860 at 892-893, Lamer J. explained it this way:
>
>> In summary, a lawyer's client is entitled to have all communications made with a view to obtaining legal advice kept confidential. Whether communications are made to the lawyer himself or to employees, and whether they deal with matters of an administrative nature such as financial means or with the actual nature of the legal problem, all information which a person must provide in order to obtain legal advice and which is given in confidence for that purpose enjoys the privileges attached to confidentiality. This confidentiality attaches to all communications made within the framework of the solicitor-client relationship, which arises as soon as the potential client takes the first steps, and consequently even before the formal retainer is established.
>
> [97] The party seeking to establish the privilege must always walk a fine line between disclosing too little information about the communications, and disclosing so much that the benefit of the privilege is effectively lost.
>
> [98] In this case, the affidavit of Mr. Belisle goes about as far as is possible. It satisfies me that the "external counsel documents" and the "in-house counsel documents" are privileged as having been made with a view to obtaining legal advice, developing information to assist in obtaining legal advice, or to discuss legal advice, all within the context of a corporate client that has retained confidential advisors . . . .

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11 The judge then turned to consider whether the asserted privilege had been waived. He identified the critical question to be whether a party can only put its state of mind in issue in such a way as to impliedly waive solicitor-client privilege if that state of mind relates to the party's understanding of its legal position in a way that is material to the lawsuit. He observed that the leading cases dealt with discrete solicitor-client communications that may or may not relate to the issues raised. He viewed this case differently because the pleadings raise a party's state of mind in the form of reliance on professional advice in the context of a complex decision that had a great deal of input.

12 The judge viewed the authorities as exemplifying a concern with whether the legal assertions of the party asserting the privilege make it unfair for that party to retain the benefit of the privilege. After examining the authorities, particularly *Creative Career Systems Inc. v. Ontario*, 2012 ONSC 649 (Ont. S.C.J.), and *Roynat Capital Inc. v. Repeatseat Ltd.*, 2015 ONSC 1108 (Ont. Div. Ct.), he chose to follow the reasoning in *Roynat* found at paras. 58, 59 and 84 of that decision:

> [58] I am of the view that the principles at para. 30 of *Creative Career Systems* can be adapted to appropriately apply to this negligent misrepresentation claim and the question of reliance. Applying the two step test, this negligent misrepresentation claim advanced by the plaintiffs makes (1) the presence of legal advice relevant to the plaintiffs' allegation of reliance; and (2) the party who received the legal advice [in this case the plaintiffs] made the receipt of the legal advice an issue in this claim as the plaintiff must prove that relying on the defendants' alleged representations was reasonable. If Cassels provided the plaintiffs with legal advice on this issue to the contrary to the position alleged in this claim, the plaintiffs' reliance would not be reasonable.
>
> [59] The line of cases relied upon by the defendants confirms that there are limited circumstances where waiver of solicitor client privilege may apply: if a party places its state of mind in issue, alleges reliance on representations made by the adverse party, and obtained legal advice with respect to that representation. I do not read *Creative Career Systems* as inconsistent with this analysis. Alternatively, I agree with the defendants' argument that *Creative Career Systems* was dealing with a different issue, and therefore the two step test outlined in para. 30 of that decision needs to be interpreted to be consistent with established law.
>
> [84] The principles of fairness and consistency temper and guide when waiver of privilege is deemed to occur. Whether fairness and consistency require implied waiver of privilege is case specific and factually dependent. The court provides an important gatekeeper function to avoid inappropriate requests for disclosure, balancing fairness with the importance of solicitor client privilege. Deemed waiver and disclosure will be limited to circumstances where the relevance of the evidence in question is high, and the principles of fairness and consistency require disclosure to allow a party to adequately defend.

13 The judge stated his conclusion as follows:

> [121] After considering these authorities, I am unable to agree with Soprema's position that waiver cannot be implied unless it has, by its pleadings, put its understanding of its legal position squarely in issue. What matters, as I understand the authorities, is whether Soprema has put its state of mind in issue in a manner that makes the privileged communications in question highly relevant to that state of mind, in that there is a clear nexus between the two. It is that nexus, that relevance, that implies the waiver, where required by fairness and consistency. As the court noted in *Roynat*, this question is case specific and factually dependent.
>
> [122] On the specific facts of this case, I am satisfied that an implied waiver does arise, and is required by fairness and consistency. This is because by alleging reliance on the representations of Wolrige, which of necessity must be reasonable reliance, Soprema has put its state of mind in issue "in such a way" as to make the privileged communications it received concerning its decision highly relevant. The question is not its understanding about its legal position *per se*, but rather upon what basis it decided to act when it was allegedly induced to act. The types of privileged communications outlined by Mr. Belisle, including advice from Mallette and others concerning the

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> decision, are of significant importance to this issue. To leave Wolrige to defend the allegations of reliance without access to these communications would confer an unfair litigation advantage on Soprema.

14 Although privilege had been waived, it had not been waived over all communications during the material period. He reasoned:

> [125] It follows that a more surgical approach is both required in law and justified on the evidence. That is the essence of the "gatekeeper function" referred to in *Roynat*. The extent of the waiver that fairness and consistency require in this case is confined, as I see it, to those privileged communications generated between May 28 and July 13, 2012, that concern or discuss:
>
> • the receipt, extent and content of the information received by Soprema or its advisors that is alleged to constitute what are defined in the amended notice of civil claim as the "2012 Audit Representations", the "Soprema Representations" and the "Mallette Representations" (collectively, the "defined representations");
>
> • the understanding of Soprema or its advisors of the nature and reliability of the information received from Wolrige concerning the defined representations;
>
> • the basis upon which Soprema exercised its decision to exercise its option;
>
> • what reliance Soprema should, could or did place upon the defined representations;
>
> • whether Wolrige had acted negligently in relation to the information that was the subject of the defined representations, or in a manner that raised concerns about the accuracy and reliability of such information; and
>
> • the factors taken into account, or which should be taken into account, by Soprema in deciding whether to exercise its option.

On Appeal

15 Soprema contends that the judge applied the wrong test in deciding whether it had impliedly waived privilege. It says that it is a necessary condition of implied waiver that a party voluntarily put in issue its understanding of its legal position or relies on the fact that it has or has not received legal advice as an element of its claim. Only then do principles of consistency and fairness come into play to compel the implication that privilege has been waived. Soprema argues that the judge failed to follow the principles laid out in such seminal cases as *Doman Forest Products Ltd. v. GMAC Commercial Credit Corp. - Canada*, 2004 BCCA 512 (B.C. C.A.), and he erred in holding that implied waiver will be found whenever the privileged advice can be assumed to be highly relevant to the claim of reliance, and fairness and consistency require disclosure.

16 The judge's conclusion that the documents in issue are subject to solicitor-client privilege is not in issue on this appeal. We must proceed on the basis that the documents are protected by solicitor-client privilege. The only issue is whether the judge correctly identified and applied the test for implied waiver of privilege. This is a question of law to be evaluated by a standard of correctness.

17 Before turning to this question, it is important to recall that the action sounds in negligent misrepresentation. It is, of course, evident that to make out that cause of action, Soprema must prove reliance on the alleged misrepresentation as a matter of fact in accordance with the test articulated, for example, in *Kripps v. Touche Ross & Co.* (1997), 33 B.C.L.R. (3d) 254, [1997] 6 W.W.R. 421 (B.C. C.A.) at para. 103, namely, that the misrepresentation is at least one factor which induced Soprema to act to its detriment. As *Kripps* makes clear, reliance may be established by inference "where the misrepresentation in question is one which was calculated or which would naturally tend to induce the plaintiff to act upon it . . . " (at para. 103). The onus of rebutting the inference of reliance rests on the representor. Further, Soprema must establish that its reliance was objectively reasonable.

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18 It follows that a claim of negligent misrepresentation necessarily puts in issue a plaintiff's "state of mind" both in respect of whether there was reliance in fact and, if so, whether that reliance was reasonable. It may often be that a party has received legal advice before entering the transaction, either about the transaction generally or, more specifically, about what it subsequently claims is the misrepresentation.

19 The parties here listed documents in accordance with the principle in *Cie Financiere et Commerciale du Pacifique v. Peruvian Guano Co.* (1882), 11 Q.B.D. 55 (Eng. C.A.). This, of course, incorporates a much broader standard of relevance than the starting point for disclosure under the *Supreme Court Civil Rules*, B.C. Reg. 168/2009, which focuses on "materiality". The claim for privilege amounts to an acknowledgement by Soprema that the privileged documents are "relevant" in accordance with the *Peruvian Guano* principle, because otherwise there would have been no obligation to list them. It cannot be inferred, however, simply from the fact that they have been listed that they satisfy a more rigorous test of materiality or that they would be admissible at trial. It follows that it is speculative to conclude that the documents are "highly relevant" to Soprema's state of mind. The judge addresses this concern, in my view, by identifying the criterion of relevance set out above at para. 13. It is possible that none of the documents would fall into the categories identified in his order. The order may be viewed as stipulating that privilege is deemed to have been waived only over documents falling into these categories.

Discussion

20 I turn now to focus on the test for implied waiver.

21 Although the law books are full of cases dealing with implied waiver, it does not appear that the precise question on appeal has been authoritatively settled in British Columbia. Some support for the principle adopted by the judge can be found in the cases. Equally, much support for Soprema's contentions can also be found. Although, in my opinion, the case authority does not provide a definitive answer to the issue before us, it is helpful to review the cases to discern what guidance they offer. Ultimately the answer must be found in an application of first principles.

22 It is of course clear that waiver is implied where a party voluntarily injects its understanding of its legal position or relies on legal advice to justify its conduct, and acts in a manner inconsistent with maintaining the privilege. In this context, waiver is implied as a result of the voluntary conduct of a party even where it did not intend that result. The cases express the test in various ways. *Doman*, for example, says:

> [12] Solicitor-client privilege, which protects the fundamental civil and legal right of citizens to communicate in confidence with their lawyers, will not be lightly abrogated: *Descoteaux v. Mierzwinski*, [1982] 1 S.C.R. 860 at 875. It will, however, be considered waived when a party makes its state of mind material to its claim or its defence in such a way that to enforce the privilege would be to confer an unfair litigation advantage on the party claiming it . . .

23 *Halsbury's* expresses the test thus: waiver will be implied if a party "voluntarily takes a position in litigation that is inconsistent with the maintenance of the privilege" (*Halsbury's Laws of Canada — Evidence* (2014 reissue) at para. 178). In *Brown v. Clark Wilson LLP*, 2014 BCCA 185 (B.C. C.A.), Madam Justice Newbury, for the Court, summarized the principle derived from paras. 17 and 26 of *Doman* in the following way at para. 30: "Subsequent decisions have also made it clear that for waiver to be implied, the privilege-holder must have raised voluntarily and for his or her own benefit the issue of whether and how he or she was influenced by the solicitor's advice; and that his or her state of mind must be material to an issue in the litigation."

24 More recently in *ProSuite Software Ltd. v. Infokey Software Inc.*, 2015 BCCA 52 (B.C. C.A.), Newbury J.A. began her reasons for the majority (at para. 1) by citing *Doman* (at para. 12): "It is a well-established principle of law that 'when a party makes its state of mind material to its claim or its defence in such a way that to enforce [solicitor-client] privilege would be to confer an unfair litigation advantage on the party claiming it', the privilege will be considered waived."

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25 There are other phrasings of the test which have been stated with approval in British Columbia. For example, in *Allarcom Ltd. v. Canwest Broadcasting Corp.* (1987), 19 B.C.L.R. (2d) 167, [1987] B.C.J. No. 1977 (B.C. S.C.), Mr. Justice Gibbs, as he then was, relying on *Rogers v. Bank of Montreal*, [1985] B.C.J. No. 2116, 62 B.C.L.R. 387 (B.C. C.A.), described the principle in a way consonant with the approach of the judge in this case. Gibbs J. said (at para. 4): "The plaintiff contends that, having put their state of mind in issue by pleading that they relied upon the plaintiff's conduct to their detriment, the defendants cannot now raise the barrier of solicitor-client privilege to prevent the plaintiff from showing that the defendants had advice and opinions which effectively negate the allegation of reliance upon the plaintiff's conduct."

26 It must be acknowledged that the formulations of the test outlined above do not clearly establish that it is a necessary condition of implied waiver that a party voluntarily inject its understanding of its legal position as a material issue into the litigation. Arguably, as the judge concluded here, the state of mind could be injected into the litigation simply because it is material to an issue advanced by a party in the litigation and there is a "nexus" between the advice and the state of mind. If legal advice would be relevant to the particular "state of mind" put in issue, waiver may be implied. If that is so, it may be sufficient for waiving privilege if a party advances a cause of action of which reasonable reliance or reliance in fact is an element. This is so because a party has made its state of mind relevant, and legal advice or its understanding of its legal position is relevant to that state of mind. This is the view of the law taken by the judge in this case.

27 It is necessary then to examine the cases more closely. I say this because, as is well-known, to understand properly the scope of a legal principle one must examine statements of principle in light of the facts giving rise to them. As Madam Justice Saunders reminded us recently in *Gorenshtein v. British Columbia (Employment Standards Tribunal)*, 2016 BCCA 457 (B.C. C.A.) at para. 28:

> . . . Lord Halsbury famously explained this proposition in *Quinn v. Leathern*, [1901] A.C. 495 (H.L.) at 506, in a passage referred to recently by this court in *Cowichan Valley (Regional District) v. Cobble Hill Holdings Ltd.*, 2016 BCCA 432:
>
> > . . . there are two observations of a general character which I wish to make, and one is to repeat what I have very often said before, that every judgment must be read as applicable to the particular facts proved, or assumed to be proved, since the generality of the expressions which may be found there are not intended to be expositions of the whole law, but governed and qualified by the particular facts of the case in which such expressions are to be found. The other is that a case is only an authority for what it actually decides.

28 Adopting this approach, I am of the view it is apparent that the cases which actually find waiver typically involve a party voluntarily making its own understanding of the law, or its reliance on legal advice it received, a material issue. This can happen in myriad ways, as illustrated in *Halsbury's*. Parties may expressly raise reliance on legal advice they received as a justification or an excuse: see e.g., *R. v. Shirose*, [1999] 1 S.C.R. 565 (S.C.C.). They may assert misconduct or incompetence of their legal advisers (see e.g., *R. v. Dunbar*, [1982] O.J. No. 581 (Ont. C.A.) at paras. 68-72, (1982), 68 C.C.C. (2d) 13 (Ont. C.A.)), dispute instructions (see e.g., *Newman v. Nemes* (1979), [1978] O.J. No. 3101, 8 C.P.C. 229 (Ont. S.C.)), or seek to justify mistakes in affidavits as made by counsel (see e.g., *Souter v. 375561 B.C. Ltd.*, [1995] B.C.J. No. 2265, 130 D.L.R. (4th) 81 (B.C. C.A.)). In other cases, a party may make a deliberate partial disclosure of a privileged communication and fairness and consistency will compel waiver over the entire communication. One must be cautious, therefore, in treating statements of principle articulated in one context as applying in another, without regard to the legal principles inherent in that statement of principle. Indeed, on my review of the cases, there is a weighty argument that underlying the reasoning in those cases is the view that a party will impliedly waive privilege only if it has voluntarily put in issue its understanding of its legal position. It is in those circumstances that it would be inconsistent with the conduct of the party to maintain privilege and unfair to do so, because in those circumstances maintaining privilege would indeed confer an "unfair" litigation advantage.

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29 There is another category of "waiver" cases which turn on a different point. In these cases, waiver is not implied because legal advice or an understanding of legal position turns out not to be material or relevant to the issue joined between the parties. For example, Mr. Justice Smith in *Doman* at para. 20 explained *Pax Management Ltd. v. A.R. Ristau Trucking Ltd.* (1987), 14 B.C.L.R. (2d) 257, [1987] 5 W.W.R. 252 (B.C. C.A.), as turning on the proposition that what was in issue were questions of fact about the truth of certain representations. Any legal or other advice received by the bank would have been irrelevant to that issue. Indeed, as I shall explore shortly, it may well be that much of the result in *Doman* turned on this Court's appreciation that Doman's understanding of its legal position, based on the advice it had received, was not material to the issues in that litigation.

30 Modern discussion of the circumstances in which waiver will be implied and the relevant test to apply begins with *S. & K. Processors Ltd. v. Campbell Avenue Herring Producers Ltd.*, [1983] B.C.J. No. 1499, 45 B.C.L.R. 218 (B.C. S.C.). In that case, McLachlin J., as she then was, articulated the principle that waiver may be implied where fairness and consistency so require. The examples she gives to demonstrate when fairness and consistency require a finding of implied waiver are twofold. First, a party may waive privilege over part of a communication. Having done so, fairness and consistency require a finding the privilege has been waived over the entire communication. The second category of cases involved circumstances where a party relies on legal advice it received as an element of its claim or defence. Having raised legal advice, for example to justify or explain its conduct, a party cannot in fairness then be permitted to assert privilege to prevent an opposing party from exploring the validity of the claim. *S. & K.* does not explore the possibility that privilege may also be impliedly waived where advice or knowledge may be relevant to state of mind but that party has not explicitly put in issue reliance on legal advice or knowledge of the law to explain or justify its conduct. I do not think the case can be interpreted as authority for the proposition that waiver is implied in such circumstances.

31 *Rogers, supra*, is often cited as a leading case on waiver in this jurisdiction. There, a bank assigned a client into receivership. The client's principals sued the bank and the receiver contending the client had wrongfully been denied the opportunity to satisfy the demand. The bank asserted it had relied on the receiver's advice in putting the customer into receivership. The receiver denied the bank relied on its advice, and sought production of any legal advice the bank had received from its own lawyers over which the bank claimed solicitor-client privilege. Hutcheon J.A. observed (at 392):

> The issue in this case is not the knowledge of the bank. The issue is whether the bank was induced to take certain steps in reliance upon the advice from the receiver on legal matters. To take one instance, the receiver, according to the bank, advised the bank that it was not necessary to allow Abacus time for payment before the appointment of the receiver. A significant legal decision had been rendered some months earlier to the opposite of that advice. The extent to which the bank had been advised about that decision, not merely of its result, is important in the resolution of the issue whether the bank relied upon the advice of the receiver.
>
> [Emphasis added.]

32 The Court went on to examine American cases that considered implied waiver when a party has injected its state of mind into the litigation. In *Doman*, Mr. Justice Smith summarized the foundation of *Rogers*:

> [18] Thus, in *Rogers v. Bank of Montreal, supra*, the privilege was waived because the elements of waiver were present. By its pleading, the bank put in issue its knowledge of the law that was at the heart of the dispute. Since the information sought was vital to the receiver's defence against the bank's claim that it had relied on the receiver's advice, fairness and consistency required that the privilege be waived.

33 It is convenient at this point to turn to *Doman* because, in my opinion, it is a case that tends to support the view that implied waiver requires a party squarely to put in issue its reliance on legal advice or its understanding of the law as a material element of its case. It is also the case Soprema most heavily relied on. For the reasons that follow, however, I do not read *Doman* as providing an unequivocal answer to the issue we must decide.

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34 *Doman* involved an allegation that GMAC, a financier, had breached its contract (a credit agreement) with Doman by reducing the limit on a revolving line of credit. Doman alleged, after a delay in which it sought replacement financing, that GMAC had repudiated the contract by so doing and that Doman was accepting that repudiation. GMAC pleaded in defence that Doman had affirmed the contract by electing not to treat the alleged breach as a repudiation. Furthermore, although GMAC would have been entitled to treat Doman's deteriorating financial position as an Event of Default (as defined in the credit agreement), Doman alleged that GMAC had not done so and the parties continued to operate the credit arrangement as if no Event of Default had occurred.

35 On discovery, it emerged that Doman had received legal advice in relation to its delay in accepting the alleged repudiation and Doman's belief that no Event of Default had occurred under the credit agreement. GMAC applied for disclosure of the legal advice. A chambers judge ordered disclosure on the basis of implied waiver in relation to two issues:

> (a) whether the Plaintiffs had no choice but to postpone accepting the Defendant's alleged repudiation of the Credit Agreement;
>
> (b) whether the Plaintiffs believed that no event of default had occurred under the Credit Agreement . . .

36 The foundation of the order was that Doman had impliedly waived privilege because Doman had put in issue its state of mind and it was reasonable to assume that the legal advice had influenced that state of mind. The appeal to this Court was allowed.

37 The reasons of Smith J.A. canvassed the principal authorities in this province, as well as other cases, including both *Rogers*, *supra*, and *Froese v. Montreal Trust Co. of Canada*, [1993] B.C.J. No. 1529 (B.C. Master), which turned on injecting legal knowledge and advice into the litigation. The role that voluntarily putting legal knowledge in issue plays in the analysis is reflected to a degree in the following passages in which Smith J.A. discusses the postponement of an election to accept an alleged repudiation of a contract. Smith J.A. said:

> [28] Further, on the question of postponement of the election, it is not enough to constitute a waiver that Doman's pleading puts its state of mind in issue and that its state of mind might have been influenced by legal advice, as the chambers judge concluded. There must be the further element that the state of mind involves Doman's understanding of its legal position in a way that is material to the lawsuit. In other words, it must appear from the pleading that legal advice would be relevant to the particular state of mind put in issue. Otherwise, it cannot be said that Doman has put its knowledge of the law in issue and that enforcing the privilege will deprive GMAC of information necessary to defend against Doman's allegation that it acted reasonably. In my view, the chambers judge applied the passages which she quoted from the decisions in *Bank Leu Ag, supra* and *Froese v. Montreal Trust, supra* without considering this necessary element of implied waiver.

38 Later, in relation to the same question, he said:

> [31] . . . Accordingly, <u>the material issue</u> arising out of paragraphs 13 and 14 of the amended statement of claim is whether, given its financial circumstances, Doman's delay was reasonable. While this plea puts Doman's state of mind as to its financial circumstances in issue, it does not raise any issue about legal advice it may have received between September 2001 and March 2002. <u>Doman has not pleaded that it relied on any legal advice or on any representation made by GMAC as to its legal position in its attempt to explain the reasonableness of the delay</u>. Nor has it pleaded that it did not appreciate until some later time that GMAC's actions amounted to a fundamental breach. <u>In short, Doman has not put its knowledge of the law in issue and any legal advice Doman received is not relevant to the determination a trial judge will have to make as to whether its delay in accepting GMAC's purported repudiation was reasonable</u>. While it might be useful to GMAC to know the nature of Doman's legal advice, it cannot be said that this knowledge is necessary to enable GMAC to meet the allegation that Doman's actions were reasonable on the basis of financial considerations. It follows that nothing in Doman's plea in these paragraphs would support an implied waiver of the privilege.

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[Emphasis added.]

39 Although these passages emphasize voluntarily putting legal advice or knowledge in issue, some aspects of the reasoning appear to be consistent with the proposition that if legal knowledge is relevant to a material state of mind, then waiver might be implied. Further, a close reading of *Doman* demonstrates that the result turns in part, at least, on the Court's view that Doman's state of mind was not a material issue in respect of some aspects of the case. Hence, at para. 27 Smith J.A. says:

> [27] Next, Doman did not make its state of mind material by pleading that the parties conducted themselves as if no Event of Default had occurred. Paragraph 17 of the reply is Doman's response to GMAC's plea that it was authorized by the terms of the agreement to act as it did since an Event of Default had occurred - it was not advanced as a justification for the delayed election. The effect of this aspect of the pleadings is that the parties joined issue on whether GMAC's unilateral reduction of the credit limit amounted to a repudiation of the agreement or whether it was entitled by the terms of the agreement to reduce the limit. Doman's state of mind is not material to either of these issues since whether there had been an Event of Default does not depend on whether Doman did or did not believe that one had occurred. Thus, the plea in paragraph 17 of the reply that the parties acted as if no Event of Default had occurred does not make Doman's state of mind material to its claim in any way that would justify overriding solicitor-client privilege.
>
> [Emphasis added.]

40 Similarly, when addressing a pleading of estoppel (as an alternative basis for waiver) in which Doman pleaded that it relied to its detriment on GMAC's acting as if no Event of Default had occurred, the Court observed "Doman's pleading is essentially that it relied on GMAC's failure to trigger a contractual provision that it says must have been triggered for a breach to have occurred, not that it relied on GMAC's representation as to a legal state of affairs upon which Doman might have received advice from its own solicitors" (para. 35). The Court identified the material issue to be an interpretative one; namely, whether GMAC was required to trigger the provision for Doman to be in breach. Doman's state of mind was irrelevant to that issue.

41 It follows that, on one reading, *Doman* was decided principally on the basis that Doman's state of mind, even if influenced by legal advice, was not material to the issues joined in the litigation because its knowledge of the law was irrelevant to those questions. On the other hand, Doman had not voluntarily injected reliance on legal advice or its legal understanding into the litigation to explain or justify its conduct, even though it could have done so. The Court, for example, appears to have respected Doman's decision to limit its position to the financial reasonableness of postponing its election. However, I do not read *Doman* as excluding the possibility that it may be inherent in advancing certain claims that privilege is impliedly waived. I note in particular the observation at para. 34 that:

> "[f]requently, a plea of estoppel will make the party's state of mind material in a way that manifests an intention to waive solicitor-client privilege: see, e.g. *Allarcom Ltd. v. Canwest Broadcasting Corp.* (1987), 19 B.C.L.R. (2d) 167 at 170-71 (S.C.). That is because such a claim usually raises the question of whether the party asserting estoppel received legal advice from its solicitors that would negate the assertion that it relied to its detriment on the representations of the other party."

42 I have already referred to *Brown*, in which Newbury J.A. said at para. 30 that: "Subsequent decisions have also made it clear that for waiver to be implied, the privilege-holder must have raised voluntarily and for his or her own benefit the issue of whether and how he or she was influenced by the solicitor's advice; and that his or her state of mind must be material to an issue in the litigation." That case involved an express assertion by a party in a closely related proceeding that any misconduct was the result of relying on advice.

43 The last significant decision in this Court is *ProSuite Software Ltd. v. Infokey Software Inc.* That case involved a pleading of duress. As Newbury J.A. observed, the assertion of duress put the defendants' state of mind in issue with

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respect to a material fact. Ordinarily, she observed, no issue of waiver would arise. But the defendants pleaded that they had signed the agreement "without legal advice" when there was evidence that they had received legal advice some years earlier about the most significant aspect of the agreement and the central issue in the proceeding. The case turned on whether a pleading of a lack of legal advice could amount to an implied waiver and the Court concluded that it could.

44 After referring to *S. & K.*, and Sopinka, Lederman and Bryant in *The Law of Evidence in Canada* (2d ed., 1999) quoting *Wigmore on Evidence*, Newbury J.A. laid out the law in passages that bear repeating:

> [23] The foregoing passages are settled law and have been applied in numerous cases. These were reviewed recently in *Brown v. Clark Wilson LLP*, 2014 BCCA 185 at paras. 23-32. As we summarized the principle on that occasion, a court will deem privilege to be waived where a litigant "voluntarily takes a position in litigation that is inconsistent with the maintenance of the privilege" (see *Halsbury's Laws of Canada* (1 st ed., 2010) at HEV 178) or makes legal assertions that "make it unfair for the holder of the privilege to retain the benefit of the privilege." (*Brown*, at para. 26; see also *Bank Leu AG v. Gaming Lottery Corp.* (1999) 43 C.P.C. (4 th) 73 at para. 5 (S.C.J.), aff'd (2000) 132 O.A.C. 127 (Div. Ct.), quoted at para. 22 of *Doman Forest Products, supra*; *Rogers v. Bank of Montreal* (1985) 62 B.C.L.R. 387 (C.A.); *Langret Investments S.A. v. McDonnell* (1995) 13 B.C.L.R. (3d) 333 (C.A.); and *Bennett v. Chief Executive Officer, Australian Customs Service*, [2004] FCAC 237 at para. 6.)
>
> [24] Did the judge in this case apply this test? At para. 5 of her reasons, she cited a description of implied waiver given in Hubbard et al., *The Law of Privilege in Canada* (2014) as follows:
>
> > Where a party voluntarily injects into the proceeding the question of its state of mind and in so doing uses the legal advice it has received as a reason for its conduct, it waives the protection of solicitor-client privilege.
> >
> > . . .
>
> [27] It seems to me that in applying the legal description, or "test", enunciated by Hubbard, the chambers judge took an overly narrow view of the law respecting waiver — or again as Mr. Griffin contended, asked herself the wrong question. I say this for two reasons. First and most importantly, the Court did not consider whether the defendants' position was inconsistent with the maintenance of the privilege, or to put it another way, whether fairness and consistency in the litigation required that waiver be implied. Because the chambers judge concluded that legal advice received three years before the execution of the 2007 agreement was effectively irrelevant to implied waiver, i.e., that the defendants had not put in issue the nature of the advice Mr. Lounine "received or did not receive", she did not reach this stage of the analysis. But with respect, the defendants <u>had</u>, by pleading duress, put their state of mind in issue. In my view, this plea, together with the allegation of 'no legal advice', lead to the conclusion that if advice was received, fairness in the litigation requires that it be disclosed.
>
> [28] This is not to suggest that a person's general knowledge or understanding of a legal principle, obtained as the result of legal advice received in a different context, will necessarily or even usually be sufficient to result in deemed waiver. The advice must obviously be highly relevant to the litigation for the tests of "fairness and consistency" to overcome the important principle of solicitor-client confidentiality. In this instance, however, it appears the advice (assuming advice was obtained) related exactly to the central issue, or one of the central issues, of the case — Mr. Lounine's state of mind when he signed and returned the letter agreement in December, 2007.
>
> [Emphasis in original.]

45 As I read it, this judgment suggests a pleading of duress standing alone would not have been sufficient for an implied waiver of privilege, even though state of mind had been put in issue as a material fact. More was required. The party put its legal knowledge in issue by pleading that it entered the agreement without legal advice. That extra element was necessary to support the result.

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46 One final case illustrates the same issue. *R. v. Shirose* concerned the legality of a reverse sting operation. An RCMP member had consulted a Department of Justice lawyer about the legality of the operation. One issue in the case involved an application for a stay of proceedings. The legality of the operation was relevant to the application and the police officer's state of mind as to its legality and good faith in conducting it were factors in whether a stay would be granted.

47 The RCMP invoked in support of its good faith argument that it had consulted with and relied on legal advice. Unsurprisingly, the Supreme Court of Canada concluded that the RCMP had waived the right to shelter behind solicitor-client privilege. But the reason for that conclusion is telling. Justice Binnie, for the Court, wrote:

> [70] The present case presents a stronger argument for waiver than *Rogers*. The Crown led evidence from Cpl. Reynolds about his knowledge of the law with respect to reverse sting operations — he testified that he had read the Superior Court decision in *Lore*, *supra*, and was of the view that the operation in question was legal. But Cpl. Reynolds also testified, in answer to the appellants' counsel, that he sought out the opinion of Mr. Leising of the Department of Justice to verify the correctness of his own understanding. The appellants' counsel recognized that this alone was not enough to waive the privilege. Cpl. Reynolds was simply responding to questions crafted by the appellants, as he was required to do. Appellants' counsel accepted that he had no right at that point to access the communications. His comment to the judge was simply that "I certainly don't want to hear the argument that 'Oh well, the police acted in good faith because they acted on legal advice'". The critical point is that the Court did [emphasis by Binnie J.] hear that precise argument from the Crown at a later date. The RCMP and its legal advisers were explicit in their factum in the Court of Appeal, where it was argued that "regard must be had to the following considerations . . . (f) The R.C.M.P. ... consulted with the Department of Justice with regard to any problems of illegality" (emphasis added by Binnie J.). We understand that the same position was advanced to the trial judge. As *Rogers*, *supra*, shows, it is not always necessary for the client actually to disclose part of the contents of the advice in order to waive privilege to the relevant communications of which it forms a part. It was sufficient in this case for the RCMP to support its good faith argument by undisclosed advice from legal counsel in circumstances where, as here, the existence or non-existence of the asserted good faith depended on the content of that legal advice. The clear implication sought to be conveyed to the court by the RCMP was that Mr. Leising's advice had assured the RCMP that the proposed reverse sting was legal.
>
> [71] Cpl. Reynolds was not required to pledge his belief in the legality of the reverse sting operation (comparable to the bank's putting in issue its belief in the correctness of the advice it was obtaining from the receiver in *Rogers*, *supra*). Nor was it necessary for the RCMP to plead the existence of Mr. Leising's legal opinion as a factor weighing against the imposition of a stay of proceedings (which went beyond what was done in *Rogers*). The RCMP and the Crown having done so, however, I do not think disclosure of the advice in question could fairly be withheld.
>
> [Emphasis added.]

48 In my view, this case, although arising in a criminal context, strongly supports the proposition that it is not sufficient for implied waiver of privilege that a party's state of mind as to its understanding of its legal position or advice it received is relevant to a material issue. Here, even though Cpl. Reynolds' state of mind was relevant, he did not have to make his legal understanding an issue. Equally, even having received legal advice, the RCMP did not need to introduce it into the proceeding to justify police conduct. If neither of these things had happened, the assumption was that privilege would not have been waived, notwithstanding the legal advice's potential relevance.

49 In my view, the authorities in this province do not clearly preclude the approach taken by the judge, although on balance I think the weight of authority supports the proposition that a party must voluntarily inject into the litigation legal advice it received or its understanding of the law before waiver can be implied.

50 I would reach the same conclusion based on principle. The starting point of an articulation of the test for implied waiver must recognize what the Supreme Court of Canada has made clear about the importance of solicitor-client

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privilege. In *R. v. McClure*, 2001 SCC 14 (S.C.C.) at para. 35, the Court said that solicitor-client privilege "must be as close to absolute as possible to ensure public confidence and retain relevance. As such, it will only yield in certain clearly defined circumstances, and *does not involve a balancing of interests on a case-by-case basis*" (emphasis added). Furthermore, the Court said (at para. 17) that solicitor-client privilege "is part of and fundamental to the Canadian legal system. . . . [I]t has evolved into a fundamental and substantive rule of law." This view was affirmed in *Ontario (Ministry of Correctional Services) v. Goodis*, 2006 SCC 31 (S.C.C.) at paras. 20-21, where the Supreme Court of Canada made clear that communications protected by privilege should be disclosed only where "absolutely necessary", applying "as restrictive a test as may be formulated short of an absolute prohibition in every case."

51 Accordingly, one must be cautious about a test for implied waiver that does not rest on a bright line capable of identifying "clearly defined circumstances", which depends on balancing interests, and which appears to treat implied waiver as ultimately a discretionary call about trial fairness. In my opinion, the test relied on by the judge does not adequately give effect to the near absolute protection of solicitor-client privilege mandated by the Supreme Court. Rather than permitting the abrogation of privilege only in clearly defined circumstances, the recognition of the privilege becomes, at best, subject to a balancing of interests on a case-by-case basis. This, in my view, is inconsistent with more recent pronouncements both of the nature and of the importance of solicitor-client privilege.

52 This point is reinforced when one recalls the nature of the cause of action. Negligent misrepresentation will always put in issue a party's "state of mind" because reliance in fact and reasonable reliance are necessary elements of the claim. Other causes of action may well raise the same issue. Where a party has received legal advice on the subject of the transaction, its understanding of the law will always be relevant. Relevance will, it seems, inevitably drive waiver. This is not consistent with the law of privilege articulated by the Supreme Court. The judge here crafted a surgical order in the exercise of a gatekeeping function intended to balance privilege and a fair trial process. However, it is not apparent to me that the approach taken addresses the concern that, in cases involving reliance in fact or reasonable reliance, claims of privilege will always be suspect because it will always be possible to craft an order focused on materiality (rather than *Peruvian Guano* relevance) and it is precisely in those circumstances that one might think that the claim of privilege is most pressing. The test used by the judge calls into question whether solicitor-client privilege would ever be protected in a case involving reasonable reliance.

53 Where legal advice may have influenced a party's "state of mind" on a material issue, it is inevitable that upholding the privilege will confer a litigation advantage on the party claiming it because the other would be denied access to relevant information about the opposing party's state of mind. One might think that this is an inevitable result of recognizing and upholding claims of solicitor-client privilege because part of the point of privilege is to protect from disclosure communications which are otherwise material and relevant. But it does not follow from this that that litigation advantage is "unfair". I do not think one can properly describe a litigation advantage "unfair" when it results from the recognition and protection of a fundamentally important principle in the legal system. Furthermore, protecting privilege in these circumstances does not raise an issue of inconsistency because the party asserting the privilege is not relying on the advice it received to justify its conduct at the same time as it shields that advice from disclosure.

Conclusion

54 Accordingly, with respect, I have concluded that the judge applied the wrong test in determining whether solicitor-client privilege had been impliedly waived. I consider that the correct test requires a party voluntarily to put in issue legal advice or its understanding of the law, in the sense described in this judgment.

55 I would allow the appeal and set aside the order for disclosure.

***Groberman J.A.*:**

I agree

***Fenlon J.A.*:**

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I agree

Appeal allowed; order set aside.

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TAB 11

2017 ONSC 3958
Ontario Superior Court of Justice

Lavender v. Miller Bernstein

2017 CarswellOnt 10841, 2017 ONSC 3958, 282 A.C.W.S. (3d) 432

Barry Lavender (Plaintiff / Moving Party) and Miller Bernstein LLP (Defendant / Responding Party)

Edward P. Belobaba J.

Heard: June 27, 2017; June 29, 2017
Judgment: July 12, 2017
Docket: 05-CV-300430-CP

Counsel: Daniel Bach, Paul Bates, Serge Kalloghlian, for Plaintiff
Robert Staley, Gavin Finlayson, Nathan Shaheen, for Defendant

Subject: Civil Practice and Procedure; Public; Torts

MOTION by investor for partial summary judgment on liability issues in class proceeding against auditor of defunct securities dealer.

***Edward P. Belobaba J.*:**

1 This class action against the auditor of a defunct securities dealer was certified as a class proceeding in 2010. The representative plaintiff now moves for summary judgment on five of the six common issues.

2 There is no serious dispute about the availability or appropriateness of summary judgment on the facts herein. I am confident that the five common issues before the court can be decided summarily without trial.

Background

3 Buckingham Securities was a securities dealer that held the investments and savings of 1002 retail clients. On July 6, 2001, the Ontario Securities Commission ("OSC") placed Buckingham into receivership because it failed to segregate investor (class member) assets and maintain a minimum net free capital in breach of regulatory requirements. BDO Dunwoody ("BDO") was appointed receiver and manager of Buckingham's assets. Although the OSC intervened as soon as it learned of these breaches, it was too late. The unsegregated assets had been appropriated and used by Buckingham for its own purposes. The class members lost some $10.6 million. [1]

4 In 2004, the OSC initiated proceedings against Buckingham and several of its principals. The principals admitted that they failed to comply with Ontario securities law by making materially untrue statements in its 1999 and 2000 Form 9 reports. Form 9 reports were to be audited and filed each year with the OSC confirming the segregation of assets and the minimum capital. The Form 9s for fiscal years 1998, 1999 and 2000 were audited and filed by Buckingham's auditor, the defendant Miller Bernstein. [2]

5 Disciplinary proceedings were brought by the OSC and the Institute of Chartered Accountants against the defendant and Howard Kornblum, the partner who audited and filed the false Form 9s. Mr. Kornblum admitted his conduct including the falsity of the Form 9s for fiscal years 1999 and 2000, but not for fiscal year 1998.

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The class action

6 The plaintiff commenced this class action in November, 2005 on behalf of every person who had an investment account with Buckingham on July 6, 2001 when the securities dealer was placed into receivership. In addition to the main class, two sub-classes were also certified: the first for the class members who corresponded directly with the defendant about discrepancies in their investment accounts; and the second for class members who corresponded with the defendant without referring to any discrepancies in their investment accounts. The sub-classes do not figure in any of the analysis herein.

7 The plaintiff says that in each of fiscal years 1998 to 2000 the defendant auditor negligently signed off on Form 9 reports that falsely stated that Buckingham was in compliance with the segregation and minimum capital requirements. In doing so, the defendant breached the duty of care that it owed to the class members (as clients of Buckingham) causing more than $10 million in foreseeable losses for which the defendant is now liable.

8 The defendant rejects the plaintiff's characterization of what happened and asks that the common issues be answered in its favour. The defendant says the plaintiff is attempting to dress up a negligent misrepresentation claim as something else because he is unable to establish reliance; that no duty of care ("to the defendant auditor's client's clients") can be imposed on the facts of this case; that neither breach nor causation nor even damages can be established on the evidence that is before the court. The defendant asks that this motion for summary judgment be dismissed.

The common issues

9 The five common issues that provide the focus for this summary judgment motion can be restated as follows:

> (a) Was Buckingham required to segregate the cash and securities of the class member investors from its own cash and securities?
>
> (b) Did Buckingham fail to do so?
>
> (c) Did the defendant owe a duty of care to class members when it audited and filed the Form 9s?
>
> (d) Did the defendant breach this duty of care?
>
> (e) Was this breach of duty a cause of damages to the class members? If so, can such damages be determined on a class-wide basis? How should the damages be calculated?

10 There was no real dispute about the first two questions — Buckingham was required to segregate client assets and failed to do so. I will explain this in more detail shortly. Nor was there much disagreement about the causation or damages questions, once these questions were canvassed with counsel during the hearing of the motion. The primary area of disagreement was the duty of care question - whether the defendant auditor on the particular facts of this case owed a duty of care to the class members.

11 Before I turn to the five common issues, I will set out the analysis relating to the core question of duty of care.

The core dispute — duty of care

12 This is not a negligent misrepresentation case. The plaintiff is not saying that the class members relied on or even saw the Form 9s — they did not. The plaintiff's claim is in negligence *simpliciter* — that the defendant owed and breached a duty of care causing foreseeable losses for which it should now be found liable.

13 Canadian courts have explained that on certain facts it is possible for a plaintiff in a negligent misstatement case to proceed against the defendant on the basis of a simple negligence claim. For example, in *Yorkshire Trust*

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Co.,[3] Justice McLachlin, as she then was, cited with approval the following passage from a leading text on the law of misrepresentation.[4] The authors are discussing "misrepresentation giving rise to actions at the suit of persons other than the representee" and they note that "a very modern cause of action" is emerging — "the cause of action in negligence which arises from making a negligent misrepresentation in a situation in which a duty of care exists":

> In some of these situations there will be found to be a duty of care owed by the representor not only to the representee, but also to third parties; and where this is the case such a third party may have a cause of action notwithstanding that he is not the representee, and even in a case where he never had notice of the representation at all. But this cause of action, as will be seen, is not really an action for misrepresentation at all, but one *in negligence* in circumstances in which the negligence consists in making a representation without due care.[5]

14 In *Lipson v. Cassels Brock & Blackwell LLP*,[6] class members participated in an income tax reduction program which resulted in reassessments. The class members sued the law firm that provided the negligent tax opinion. The law firm argued that the plaintiff's negligence claim was a disguised negligent misrepresentation action that attempted to circumvent the reliance and causation requirements. The Court of Appeal explained why a free-standing claim for negligence could proceed:

> [T]he claim in simple negligence is distinct from [the plaintiff's] claim in negligent misrepresentation, which required proof of reliance on the opinion by individual class members in deciding to participate in the program. Framed in this way, the cause of action in simple negligence does not require a showing of reliance on the Cassels Brock opinion by individual class members. The allegation is that class members suffered damage because they participated in the program, which, but for Cassels Brock's negligent opinion, would not have been marketed by the promoters and thus not available to class members.[7]

15 Here as well, the plaintiff's negligence claim is based on the allegation that class members sustained losses which, but for the defendant's false audit of the Form 9s, would not have been sustained. If the defendant had filed accurate Form 9s documenting the regulatory breaches (or had not filed at all) the OSC, on the evidence, would in all likelihood have intervened before all the assets and monies were lost. In short, I am satisfied that on these facts and in principle that the negligence claim is appropriate.

16 The more pressing issue is whether on the facts herein the plaintiff can establish a duty of care. This is a case about an auditor's misstatement that was filed with the OSC, was never seen by the class members, and arguably caused pure economic loss to the auditor's client's clients. This is obviously not a conventional negligence case. Nor is it sufficient for the plaintiff to say that the case fits within the "negligence performance of a service" category in which courts have recognized duties of care in certain third-party-benefit situations.[8] The underlying facts in the cases that have been grouped by academic commentators under the "negligent performance of a service" category are varied and the applicable law has not yet been uniformly articulated or accepted.[9]

17 In any event, as the Supreme Court noted in *Martel*,[10] the categories of recovery in tort for pure economic loss, such as the 'negligence performance of a service' category, are "merely analytical tools" that may provide structure to the varied factual situations that can arise.[11] If the case (such as the case here) does not fall within a relationship that has been previously recognized as giving rise to a duty of care, the two-stage *Anns-Cooper*[12] analysis must be undertaken.[13]

18 The first stage of the *Anns-Cooper* analysis asks whether the facts disclose a sufficient level of foreseeability and proximity to establish a *prima facie* duty of care. The second stage of the analysis asks whether there are residual policy considerations that would justify denying liability in tort even though a *prima facie* duty of care has been established.[14] The onus at the first stage is on the plaintiff; at the second stage, on the defendant.[15]

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Stage one — prima facie duty of care

19 The first stage of the analysis, reasonable foreseeability and proximity (or neighborhood), requires the court to "evaluate the closeness of the relationship between the plaintiff and the defendant and to determine whether it is just and fair having regard to that relationship to impose a duty of care in law upon the defendant." [16] As the Supreme Court noted in *Hercules Management*, [17] the question of proximity, in essence, is "whether, as a matter of simple justice, the defendant may be said to have had an obligation to be mindful of the plaintiff's interests in going about his or her business." [18]

20 Here on the evidence, I find that the foreseeability and proximity requirements are satisfied. Even though the class members never saw or even knew, at the time, about the Form 9s, the defendant auditor as a matter of simple justice had an obligation to be mindful of the plaintiff's interests when auditing and filing the Form 9 reports with the OSC.

21 My analysis is based on the auditing standards applicable at the time and the evidence and admissions of the parties and their experts. The defendant understood that the Form 9s were used by the OSC to police the securities dealers and protect their investors. If the Form 9s indicated a breach of the segregation or minimum capital requirements, the OSC would intervene. If the defendant was negligent in its audit and filed false Form 9s, causing the OSC to believe that the securities dealer was in compliance with the regulatory requirements when the truth was otherwise, monies invested by clients of the securities dealer could well be lost. In short, the defendant (and in particular Mr. Kornblum) well understood the consequences to "its client's clients" if the segregation or capital deficiency information was misstated in the Form 9s - that a negligent audit of these Form 9s could expose the class members to the very loss that they incurred.

22 The Supreme Court explained the relationship between foreseeability and proximity in *Imperial Tobacco*: [19]

> Proximity and foreseeability are two aspects of one inquiry - the inquiry into whether the facts disclose a relationship that gives rise to a *prima facie* duty of care at common law. Foreseeability is the touchstone of negligence law. However, not every foreseeable outcome will attract a commensurate duty of care. Foreseeability must be grounded in a relationship of sufficient closeness, or proximity, to make it just and reasonable to impose an obligation on one party to take reasonable care not to injure the other. [20]

23 In my view, on the particular facts herein, a relationship of sufficient closeness has been established. The defendant was retained by Buckingham to audit and file the Form 9s. In doing this "assurance audit" for its client, the defendant had access to the individual names and investor accounts of every class member. The defendant knew the exact amounts involved, and even corresponded with some of the class members to verify that Buckingham's internal client account records were complete and accurate. Some of the class members responded to the auditor's letter and alerted the defendant to serious discrepancies between Buckingham's internal account records and the actual holdings and activity within their accounts. The defendant also knew, without being told, that even if the class members knew nothing about the Form 9s, they would reasonably expect Buckingham and its auditor to provide any information required under provincial law accurately and honestly, particularly if that information could affect their financial interests.

24 I therefore have no difficulty concluding on the particular facts of this case, that it is just and reasonable to impose a *prima facie* duty of care on the defendant auditor. Tracking the language used by the Supreme Court in *Hercules Management*, I am satisfied that "as a matter of simple justice, the defendant [had] an obligation to be mindful of the plaintiff's interests in going about his or her business." [21]

25 The plaintiff has established a *prima facie* duty of care under the first stage of the *Anns-Cooper* analysis.

Stage two — indeterminate liability

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26 The reason for stage two is especially important in cases such as this where the plaintiff's claim is for pure economic loss. The court's primary concern when imposing a duty of care in cases of pure economic loss is the spectre of indeterminate or unlimited liability. [22] Unlike physical injury or property loss claims that are almost always circumscribed, pure financial loss can materialize and spread quickly involving a wide range of direct and indirect claimants and exposing the defendant to unbounded liability. At stage two of the *Anns-Cooper* analysis, as the Court of Appeal noted in *Canadian Imperial Bank of Commerce v. Deloitte & Touche,* [23] "[t]he overriding question is whether indeterminate liability can be shown not to be a concern on the facts of a particular case." [24]

27 If the defendant can show that indeterminate liability is a genuine concern, the *prima facie* duty of care will be negated. However, if indeterminate liability cannot be established *on the facts of the particular case*, then a duty of care will be found to exist. [25]

28 The case law has made clear that indeterminate liability will not be a concern under the second stage of the *Anns-Cooper* analysis in cases where the auditor knows the identity of the plaintiff (or a class of plaintiffs) *and* where the defendant's statements are used for the specific purpose for which they were made. Indeterminate liability will not be a concern if these facts are present because the defendant's scope of liability can be circumscribed. If the plaintiff-identity and specific-purpose conditions are satisfied the *prima facie* duty of care established at the first stage of the *Anns-Cooper* analysis will not be negated and a duty of care may properly be found to exist. [26]

29 Here, on the uncontroverted evidence before me, both the plaintiff-identity and specific purpose conditions are satisfied. First, the defendant knew the names and addresses of each of Buckingham's clients at the time of its audits. It was also required, between audits, to stay informed of any major changes to Buckingham's business, such as a significant change in customers, or the value of their accounts. The defendant therefore knew of the narrowly circumscribed class of people to whom it could be liable for a negligent audit. Second, the Form 9s on the facts herein were used for the very purpose for which they were prepared - to be relied on by the OSC in protecting investor (class member) assets.

30 Further, the evidence shows that the defendant's potential monetary liability was also narrowly circumscribed. It knew its precise potential liability (the sum of all customer accounts) at the time of each audit, and it was required to stay informed of any major changes. Indeed, the plaintiff notes that the defendant's liability is actually much less today than it would have been at the time of the 2000 audit. The Form 9 for March 31, 2000 indicated that the aggregate value of customer securities at that time was approximately $47.7 million — more than four times the $10.6 million that was lost.

31 One final point. The defendant's submission that it has statutory immunity under s. 141(2) of the OSA because it "intended" to comply with securities laws does not succeed. Section 141(2) provides as follows:

> No person or company has any rights or remedies and no proceedings lie or shall be brought against any person or company for any act or omission of the last-mentioned person or company done or omitted in compliance with Ontario securities law.

32 This court made clear in *Sells v. Manulife Securities Inc.* [27] that the immunity under s. 141(2) is only available to a defendant for acts or omissions that are "in compliance with Ontario securities law." [28] The defendant's filing of false Form 9s was obviously not in compliance with the OSA or the regulations thereunder, and thus s. 141(2) does not apply.

33 In sum, I find that a *prima facie* duty of care has been established and has not been negated by any policy concerns of indeterminate liability. I find on the facts of this particular case that the defendant owed a duty of care to the class members.

34 I will now answer each of the five common issues.

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The common issues answered

(a) Did the Securities Act, R.S.O. 1990, c. S.5 and the regulations thereunder require Buckingham to segregate the cash and securities of its clients from its own cash and securities?

35 The answer to (a) is yes.

36 The evidence is undisputed and the parties agree. As a registered securities dealer, Buckingham was required under the OSA and the regulations thereunder to segregate and hold in trust the cash and securities of the class on a client by client basis at all times.

(b) Did Buckingham fail to segregate its clients' cash and securities in violation of the OSA and, if so, when did Buckingham fail to do so?

37 The answer to (b) is yes. Buckingham failed to segregate its clients' cash and securities at all times during its operation.

38 The evidence shows that Buckingham never segregated its clients' cash and securities. In their settlement agreements with the OSC, Buckingham and its principals admitted that during the entire period of its registration as a securities dealer "Buckingham failed to segregate fully paid or excess margin securities owned by its clients and held in Buckingham's omnibus accounts with other brokerage firms." Mr. Kornblum also admitted that Buckingham failed to segregate at the time of the 1999 and 2000 Form 9s and he testified that Buckingham was "consistent" in the way it handled segregation prior to March 2000 (in other words, it did not segregate).

(c) Did the defendant owe a duty of care to the class and/or one or more of the sub-classes and what is the nature and extent of that duty?

39 The answer to (c) is yes. Under the *Anns-Cooper* analysis, as set out above, the defendant owed a duty of care to the class to conduct an audit of Buckingham's Form 9 reports with the skill and care of a competent practitioner.

(d) If the answer to (c) is yes, did the defendant breach that duty of care to the class and/or one or more of the sub-classes, either negligently or recklessly?

40 The answer to (d) is yes.

41 The defendant signed audit reports addressed to the OSC for fiscal years 1998, 1999 and 2000, falsely stating that its examinations of the Form 9s "were made in accordance with generally accepted auditing standards and accordingly included such tests and other procedures as we considered necessary in the circumstances, including the audit procedures prescribed by the Ontario Securities Commission." The defendant has admitted that it breached its duty of care in the 1999 and 2000 Form 9 audits. The uncontested opinion of the plaintiff's expert is that the defendant also breached its duty of care in the 1998 Form 9 audit. The defendant has not filed any expert evidence to rebut that opinion.

(e) If the answer to (d) is yes, was the defendant's breach of that duty a cause of damages to all of the class and/or all of one or more of the sub-classes?

42 The answer to (e) is yes.

43 The uncontested evidence is that shortly after the 1998 Form 9 was submitted, Buckingham was failing to segregate but had adequate net free capital. This means that if the OSC had intervened at that point to correct the segregation deficiency there would have been enough money to pay out all of Buckingham's clients in full. In other words, says the plaintiff, if the defendant had conducted a proper audit in 1998 there would have been no losses, based upon his

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admission that there were sufficient funds in 1998 and on the likelihood that the OSC would have (at a minimum) imposed segregation, protecting client assets on a go-forward basis.

44 In any event, common issue (e) only asks whether the defendant's breach of the duty of care was *a* cause of the damages sustained by the class. It cannot be disputed that the defendant's filing of the false Form 9s was at least *a* cause of the losses sustained by the class members.

(e)(1) If the answer to (e) is yes, can such damages be determined on a class wide basis in respect of the class and/or one or more of the sub-classes?

45 The answer to (e)(1) is no.

46 The plaintiff has a "corrected spreadsheet" prepared by the Receiver that shows each individual class member's loss as of July 6, 2001. However, this corrected spreadsheet is not in the evidence that is before the court. There is therefore no evidence of the class members' actual losses, whether on an individualized or class-wide basis, and no proposed methodology for making this determination. The expert reports purporting to estimate aggregate losses do not assist because actual loss is needed to establish liability in a tort claim and aggregate damages cannot be used to establish actual loss/liability. [29] The answer to common issue (e)(1) must therefore be no.

47 The plaintiff has indicated that it may bring a follow up motion for summary judgment based on this corrected spreadsheet. The defendant has cautioned the plaintiff that if such a motion is brought, it will question both the contents of the corrected spreadsheet and the assessment of each class member's alleged loss. Needless to say, this motion is not before me today.

(e)(2) If the answer to (e)(1) is yes, how should the damages to be payable by the defendant be calculated?

48 Given the answer to (e)(1), there is no need to answer (e)(2).

Conclusion

49 The common issues, with the exception of damages, are answered in favour of the plaintiff. Buckingham Securities was required to segregate the class members' cash and securities and failed to do. The defendant owed a duty of care to the class members when it audited and filed the Form 9s and breached this duty of care. This breach of duty was a cause of the losses that were sustained herein. However, the class members' losses cannot be determined on the record before the court, whether on an individual or class-wide basis.

50 The plaintiff has indicated that he may bring a follow-up motion based on the "corrected spreadsheet" so that these losses may be determined - but this remains to be seen.

Disposition

51 The motion for summary judgment on the five common issues is granted. Common issues (a), (b), (c), (d) and (e) are answered "yes". Common issue (e)(1) is answered "no" and common issue (e)(2) is not answered.

52 If the parties cannot agree on costs on a partial indemnity basis, I would be pleased to receive brief written submissions — from the plaintiff within 14 days and from the defendant within 14 days thereafter. The defendant is reminded that if it intends to challenge the reasonableness of the plaintiff's dockets, it should provide a certified copy of its own dockets showing the time expended on this motion.

53 My thanks to counsel on both sides for their assistance.

Motion granted.

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Footnotes

1 The actual amount of the loss will need further clarification because of a court-approved distribution by the Receiver to class members in 2005 in the amount of $2.3 million. There are questions about the interest owing at that point on the $10.6 million and the consequent value of the 2005 distribution. For the purposes of the narrative herein and for ease of reference, I will continue to use the $10.6 million amount to describe the class members' overall loss as of July 6, 2001.

2 The defendant auditor at the time in question was Miller Bernstein & Partners LLP not the named defendant Miller Bernstein LLP. The parties have advised that they are trying to resolve the misnomer matter on consent and are optimistic that this will be done shortly.

3 *Yorkshire Trust Co. v. Empire Acceptance Corp.*, [1986] B.C.J. No. 3254 (B.C. S.C.).

4 Spencer Bower and Turner, *The Law of Actionable Misrepresentation*, (3rd ed.), at 395-6.

5 *Ibid.*, at para. 12.

6 *Lipson v. Cassels Brock & Blackwell LLP*, 2013 ONCA 165 (Ont. C.A.).

7 *Ibid.*, at paras. 96 to 98.

8 See generally Feldthusen, *Economic Negligence: The Recovery of Pure Economic Loss*, (6th ed., 2012) at 129 *et seq.* and the case law discussed therein.

9 *Ibid.*

10 *Martel Building Ltd. v. R.*, [2000] 2 S.C.R. 860 (S.C.C.).

11 *Ibid.*, at para. 45.

12 *Anns v. Merton London Borough Council*, [1978] A.C. 728 (U.K. H.L.); *Cooper v. Hobart*, 2001 SCC 79 (S.C.C.).

13 *Childs v. Desormeaux*, [2006] 1 S.C.R. 643 (S.C.C.) at para. 15; *Knight v. Imperial Tobacco Canada Ltd.*, [2011] 3 S.C.R. 45 (S.C.C.) at para. 38.

14 *Imperial Tobacco*, *supra*, note 13, at para. 39.

15 *J. (J.) (Litigation guardian of) v. C. (C.)*, 2016 ONCA 718 (Ont. C.A.) at para. 34.

16 *Cooper*, *supra*, note 12, at para. 34.

17 *Hercules Management Ltd. v. Ernst & Young*, [1997] 2 S.C.R. 165 (S.C.C.).

18 *Ibid.*, at para. 28.

19 *Imperial Tobacco*, *supra*, note 13.

20 *Ibid.*, at para. 41.

21 *Hercules Management*, *supra*, note 17, at para. 28.

22 *Mandeville v. Manufacturers Life Insurance Co.*, 2014 ONCA 417 (Ont. C.A.) at para 173; *Hercules Management supra*, note 17, at para 31.

23 *Canadian Imperial Bank of Commerce v. Deloitte & Touche*, 2016 ONCA 922 (Ont. C.A.).

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24 *Ibid.*, at para. 66.

25 *Hercules Management*, *supra*, note 17, at 41.

26 *Ibid.*, at paras. 30 and 37; *Deloitte*, *supra*, note 23, at para. 55.

27 *Sells v. Manulife Securities Inc.*, 2014 ONSC 715 (Ont. S.C.J.).

28 *Ibid.*, at para. 38.

29 *Pro-Sys Consultants Ltd. v. Microsoft Corp.*, 2013 SCC 57 (S.C.C.) at paras. 128 and 135. Also see the discussion in *Kalra v. Mercedes Benz*, 2017 ONSC 3795 (Ont. S.C.J.) at paras. 48-50.

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TAB 12

2011 ONCA 460
Ontario Court of Appeal

Agribrands Purina Canada Inc. v. Kasamekas

2011 CarswellOnt 5034, 2011 ONCA 460, [2011] O.J. No. 2786, 106 O.R. (3d) 427, 203 A.C.W.S. (3d) 753, 278 O.A.C. 363, 334 D.L.R. (4th) 714, 86 C.C.L.T. (3d) 179, 87 B.L.R. (4th) 1

Agribrands Purina Canada Inc. (Plaintiff / Appellant) and Walter Kasamekas and Sherry Kasamekas, Raymond Joseph Jackson and Savitri Jackson (Defendants / Respondents)

Walter Kasamekas and Sherry Kasamekas, Raymond Joseph Jackson and Raywalt Feed Sales (Plaintiffs by Counterclaim / Respondents) and Agribrands Purina Canada Inc., Ren's Feed and Supplies Limited, Walter Rendell Job, McGrath Farms Inc., Edward James McGrath Farms Ltd., E.J.M. Farms Ltd. and The Estate of Edward James McGrath (Defendants by Counterclaim / Appellants)

S.T. Goudge, E.E Gillese, R.G. Juriansz JJ.A.

Heard: February 14, 2011
Judgment: June 20, 2011 *
Docket: CA C51618, C51637

Proceedings: varying *Agribrands Purina Canada Inc. v. Kasamekas* (2010), 2010 CarswellOnt 98, 2010 ONSC 166 (Ont. S.C.J.)

Counsel: Kirk F. Stevens, Gerard V. Thompson, for Appellants
W. Graydon Sheppard, Marc Munro, for Respondents

Subject: Torts; Contracts; Civil Practice and Procedure; Corporate and Commercial; Estates and Trusts

APPEAL by defendants by counterclaim from judgment reported at *Agribrands Purina Canada Inc. v. Kasamekas* (2010), 2010 CarswellOnt 98, 2010 ONSC 166 (Ont. S.C.J.), finding them liable for tort of unlawful conduct conspiracy and breach of contract, and awarding plaintiff general and punitive damages plus prejudgment interest.

***S.T. Goudge J.A.*:**

Introduction

1 After an eleven day trial, the respondents, Walter Kasamekas ("Kasamekas"), Raymond Jackson ("Jackson"), and Raywalt Feed Sales Ltd. ("Raywalt"), recovered judgment for general damages and prejudgment interest in the amount of $2,096,406 against the appellants Agribrands Purina Canada Inc. ("Purina"), Ren's Feed and Supplies Ltd. ("Ren's"), Walter Rendell Job ("Job") and The Estate of Edwards James McGrath ("McGrath"). The respondents also recovered punitive damages of $30,000 against Purina. Finally, they were awarded costs of $175,000.

2 The trial judge found the appellants liable to the respondents for the tort of unlawful conduct conspiracy. He also found Purina in breach of its contract with Raywalt. He assessed damages on the same basis for both causes of action.

3 The appellants appeal the finding of unlawful conduct conspiracy. They also say that the trial judge made errors in calculating damages for that tort and in the rate he applied for prejudgment interest. While Purina does not contest

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the breach of contract finding against it, it does contest the method the trial judge used to calculate the damages for that breach. Finally, Purina appeals the finding of punitive damages against it.

4 For the reasons that follow, I would allow the appeal on each of these issues except punitive damages and the alleged errors in calculating the tort damages. I would therefore amend the trial judgment to provide that Raywalt recover damages for breach of contract by Purina on the basis described below, with prejudgment interest calculated on the basis described below. The respondents' claims for conspiracy must be dismissed.

The Trial Judgment

5 The basic facts are not in dispute. Ren's was a well established dealer of Purina livestock feed and pet food. However, in 1990 Purina discovered that Ren's was also purchasing feed from one of its competitors and selling it as feed for laboratory animals in breach of its dealership agreement with Purina. As a consequence, Purina terminated Ren's dealership in July 1990.

6 Walter Kasamekas, who was a Purina employee, and his brother Raymond Jackson saw an opportunity to set up Raywalt as a Purina dealership to take over Ren's territory. Raywalt and Purina concluded a dealership agreement in February 1991, pursuant to which Purina agreed not to appoint any other dealer in Raywalt's territory, previously Ren's territory.

7 Raywalt opened for business in mid-March 1991. However, despite giving Raywalt territorial exclusivity, Purina continued to supply feed to Ren's until the end of April 1991. This enabled Ren's to sell to its former customers in what was now Raywalt's territory. When Purina finally ended this practice, Ren's got McGrath, who was a friend and the Purina dealer in a neighbouring territory, to supply Ren's with Purina feed at dealer prices. This allowed Ren's to continue to sell Purina feed in Raywalt's territory. Purina knew of, condoned and indeed approved of this arrangement. Purina provided McGrath with feed for resale to Ren's. As a result, Raywalt's business was not nearly as profitable as projected and its cash flow problems caused it to cease business at the end of January, 1992.

8 After setting this factual scene, the trial judge turned first to Purina's liability for breach of its contract with Raywalt. He concluded that, by supplying McGrath with feed knowing that McGrath would sell it to Ren's at dealer prices for sale in Raywalt's territory and by approving this arrangement, Purina breached its contract with Raywalt. Purina does not appeal this finding.

9 He then addressed the method of calculating damages for that breach, in particular whether the damages were time limited by the terms of the contract. Two of its provisions were relevant. The first provided that the dealership agreement was for two years but would automatically renew unless either party gave notice of cancelation. The second allowed either party to cancel the contract at any time by giving 60 days notice.

10 The trial judge concluded that there was an implied duty of good faith on Purina in its contract with Raywalt, that Purina had acted in bad faith and that it could therefore not rely on the provision allowing it to terminate the contract on 60 days notice. On this basis, the trial judge distinguished *Hamilton v. Open Window Bakery Ltd.* (2003), [2004] 1 S.C.R. 303 (S.C.C.). In considering *Hamilton*, he said at para. 100, "[T]he trial judge specifically found that the defendant *had acted in good faith* at all material times" (emphasis in original). At para. 108, he concluded, "The case has no application here because the foundation of good faith that was present in that case is evidently absent in this case."

11 Instead of applying *Hamilton*, the trial judge engaged in an inquiry into what would have happened if Purina had not breached its contractual obligation. He found that the only reasonable conclusion available on the evidence was that the contract would have continued indefinitely. He found that Purina dealerships were typically of long duration. In this case, it would have been because no steps would have been taken to terminate it. By its terms, the dealership agreement would therefore have continued automatically.

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12 In addition, he concluded that, because of Purina's conduct, the doctrine of unconscionability applied to prevent Purina from relying on the time limiting provisions in the dealership agreement.

13 For these reasons, the trial judge based his quantification of damages for breach of contract on the premise that Purina's contract with Raywalt would have continued indefinitely.

14 He then moved to the civil conspiracy issue. The respondents did not advance the branch of this tort that requires the plaintiff to demonstrate that the defendants' primary purpose was to cause injury to the plaintiff, whether by lawful or unlawful means. Rather, the respondents' argument was that the appellants engaged in the tort of unlawful conduct conspiracy, that is, their conduct, done in concert, was unlawful and they knew or should have known that injury to the respondents was likely to result.

15 The trial judge found that the appellants acted in concert, and while their predominant purpose was not to injure the respondents, their conduct was directed at the respondents, and it was reasonably foreseeable that serious economic injury to the respondents would and did result.

16 The central issue was whether their conduct was "unlawful". The trial judge found that the appellants did not appear to have committed a crime, or any other tort than unlawful conduct conspiracy. Nor had they infringed a guaranteed constitutional right. Relying primarily on *Reach M.D. Inc. v. Pharmaceutical Manufacturers Assn. of Canada* (2003), 65 O.R. (3d) 30 (Ont. C.A.) [hereinafter *Reach*], he found that the ambit of unlawful conduct required by this tort extends beyond strict illegality. He put it this way at para. 127:

> The newer decisions confirm that the ambit of "illegal conduct" extends beyond strict illegality for the purposes of proving the existence of tortious conduct. It includes conduct that the defendant "is not at liberty" or "not authorized" to engage in, whether as a result of law, a contract, a convention or an understanding.

17 His assessment of the appellants' conduct against this standard was as follows at paras. 132-134:

> It was unlawful and unauthorized conduct from Purina's perspective because Purina had a commercial obligation of good faith and was contractually bound to support Raywalt as its dealer. More importantly, Purina had no authority or entitlement to permit Purina feed products to continue to be sold by Ren's at dealer pricing just to ensure that its decision to terminate the Ren's dealership would not result in a reduction of its market share. It effectively licensed Ren's through McGrath to sell products in a geographic area that was reserved to another dealer, both as *de facto* dealers of Purina horse feeds.
>
> It was unlawful and unauthorized conduct from McGrath's perspective because he had no authority under his Dealership Agreement with Purina to establish a sub-dealership and to receive dealer rebates that reduced the product cost to dealer level "white list" pricing where his sub-dealer was selling Purina feed products in territory that had been assigned to another dealer.
>
> It was unlawful and unauthorized conduct from Walter Rendell Job's and Ren's Feeds perspective because Ren's was not entitled to be able to obtain Purina feed products for resale at the advantageous pricing available only to authorized Purina dealers. The illegality lies in Purina and McGrath effectively licensing Ren's to deal in the Raywalt territory.

18 The next issue was the assessment of damages. The trial judge concluded that there was no material difference in the damages to which the respondents were entitled whether assessed for Purina's breach of contract or for the tort of unlawful conduct conspiracy. He said this at para. 158:

> To my mind, as will be evident from the foregoing, in the absence of effective contractual language limiting liability, the assessment of damages in both tort and contract in this case should be and is essentially the same. Any loss suffered by the plaintiffs that was reasonably foreseeable at the time of the breach is properly compensable.

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19 The trial judge found that the appellants' actions caused the respondents to lose their business. He determined that damages should reflect the going concern value of Raywalt at the time, which he calculated by assessing what the net profit of the business would have been in its second year of operation had it continued beyond January 1992. He then applied a three times earnings multiple. The result was a damage award of $954,213 for Purina's breach of contract and the appellants' conspiracy.

20 The trial judge applied a prejudgment interest rate of 6.65% to this amount. Because eighteen years had passed since the cause of action arose in 1992, this added an additional $1,142,193. In supplementary reasons released on May 3, 2010, the trial judge noted that he selected that rate because it was "the average rate applicable for the entire 1992 calendar year". He declined to use the rate of 5.1%, which was the bank rate at the start of the third quarter of 1992, the quarter in which the respondents filed their claim.

21 Finally, the trial judge dealt with punitive damages. He reiterated that Purina's breach of its exclusivity contract with Raywalt was also answerable in the tort of conspiracy. He found that, if Purina's participation in that tort was not enough to justify the imposition of punitive damages, the breach of its implied duty of good faith to Raywalt was the second respect in which its conduct constituted an actionable wrong. Having found this precondition to be met, the trial judge based his justification for punitive damages on Purina's conduct. He found it was "the very antithesis of acting in good faith".

22 In the result, the trial judge ordered that the respondents recover $2,096,406 jointly and severally from the appellants, inclusive of prejudgment interest, that Purina pay punitive damages of $30,000 and that the respondents receive trial costs fixed at $175,000.

Analysis

23 The appellants raise five issues. I will deal with each in turn.

First Issue — The Unlawful Conduct Conspiracy

24 The seminal case in Canada on the tort of civil conspiracy is *Canada Cement LaFarge Ltd. v. British Columbia Lightweight Aggregate Ltd.*, [1983] 1 S.C.R. 452 (S.C.C.). Speaking for the court, Estey J. described at p. 471 two categories of conspiracy recognized by Canadian law:

> Although the law concerning the scope of the tort of conspiracy is far from clear, I am of the opinion that whereas the law of tort does not permit an action against an individual defendant who has caused injury to the plaintiff, the law of torts does recognize a claim against them in combination as the tort of conspiracy if:
>
>> (1) whether the means used by the defendants are lawful or unlawful, the predominant purpose of the defendants' conduct is to cause injury to the plaintiff; or,
>>
>> (2) where the conduct of the defendants is unlawful, the conduct is directed towards the plaintiff (alone or together with others), and the defendants should know in the circumstances that injury to the plaintiff is likely to and does result.
>
> In situation (2) it is not necessary that the predominant purpose of the defendants' conduct be to cause injury to the plaintiff but, in the prevailing circumstances, it must be a constructive intent derived from the fact that the defendants should have known that injury to the plaintiff would ensue. In both situations, however, there must be actual damage suffered by the plaintiff.

25 This case deals with the second category, namely unlawful conduct conspiracy. The first does not apply because there was no finding that the predominant purpose of the appellants' conduct was to cause injury to the respondents. The respondents did not advance that proposition at trial.

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26 For the appellants to be liable for the tort of unlawful conduct conspiracy, the following elements must therefore be present:

a) they act in combination, that is, in concert, by agreement or with a common design;

b) their conduct is unlawful;

c) their conduct is directed towards the respondents;

d) the appellants should know that, in the circumstances, injury to the respondents is likely to result; and

e) their conduct causes injury to the respondents.

27 In this court, the appellants challenge only the finding that their conduct was unlawful. In particular, while they acknowledge that Purina's breach of its contract with Raywalt was unlawful, they say that the conduct of Ren's and McGrath was in no sense unlawful, and that therefore this element of the tort was not made out. Civil conspiracy cannot be established if only one conspirator acts unlawfully.

28 What, then, are the requirements for unlawful conduct for the purposes of this tort? Most obviously, it must be unlawful conduct by each conspirator: see *Bank of Montreal v. Tortora* (2010), 3 B.C.L.R. (5th) 39 (B.C. C.A.). There is no basis for finding an individual liable for unlawful conduct conspiracy if his or her conduct is lawful, or alternatively, if he or she is the only one of those acting in concert to act unlawfully. The tort is designed to catch unlawful conduct done in concert, not to turn lawful conduct into tortious conduct. The trial judge applied this requirement, and found that each of the appellants had committed an unlawful act.

29 To determine what sort of conduct qualifies as "unlawful" the trial judge looked to the jurisprudence dealing with the tort of intentional interference with economic relations.

30 The trial judge concluded from the intentional interference cases that "unlawful conduct" includes conduct that the defendant "is not at liberty" or "not authorized" to engage in, whether as a result of law, a contract, a convention or an understanding.

31 With respect, I do not think the jurisprudence goes that far. In *Reach*, this court found the tort of intentional interference with economic relations to be made out because actions by the defendant, a voluntary association, that caused its members to stop advertising with the plaintiff, constituted unlawful means directed at third parties, which then caused them to injure the plaintiff. The court was clear that these actions were beyond the lawful authority that the defendant had under its constitution, and were therefore actions beyond the defendants powers and done without jurisdiction. They could be set aside by the court at the behest of the third parties, its members. While the court made reference to the judgment of Lord Denning in *Torquay Hotel Co. v. Cousins* (1968), [1969] 2 Ch. 106 (Eng. C.A.), it explicitly declined to decide how far Lord Denning's concept of "unlawful conduct" as "an act which [the defendant] is not at liberty to commit" might extend. *Reach* was a case of conduct that was wrong in law. I do not think that it provides a basis for the expansive interpretation used by the trial judge as any "conduct that the defendant is not at liberty or not authorized to engage in, whether as a result of law, a contract, a convention or an understanding."

32 Since *Reach*, this court's jurisprudence on the tort of intentional interference with economic relations has, if anything, tightened the scope of conduct considered unlawful. In *Drouillard v. Cogeco Cable Inc.* (2007), 86 O.R. (3d) 431 (Ont. C.A.), the defendant's conduct in not following its internal corporate policy but instead acting in bad faith did not amount to unlawful means. In *Correia v. Canac Kitchens* (2008), 91 O.R. (3d) 353 (Ont. C.A.), this court approved of Lord Hoffman's majority reasons in *OBG Ltd. v. Allan* (2007), [2008] 1 A.C. 1 (U.K. H.L.), in which he required unlawful conduct against a third party to be conduct that is actionable by the third party for the purposes of the tort of intentional interference with economic relations. This court reiterated this principle in *Alleslev-Krofchak v. Valcom Ltd.*,

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2010 ONCA 557 (Ont. C.A.), while recognizing that the delineation of actionability remained to be fully defined. It was unnecessary to do so in that case because the unlawful conduct relied on was clearly actionable as a matter of private law.

33 What is clear from this jurisprudence is that, to constitute unlawful conduct for the purposes of the tort of intentional interference, the conduct must be actionable. It must be wrong in law. Conduct that is merely not authorized by a convention or an understanding is not enough. On this standard, the approach used by the trial judge was simply too broad.

34 Moreover, reliance on the tort of intentional interference to supply the definition of "unlawful conduct" for the tort of civil conspiracy does not recognize that these two economic torts have evolved separately, and thus each have developed their own concept of unlawful conduct.

35 The court should therefore be cautious of turning away from the history of this separate evolution simply to achieve a unified theory for the economic torts. Indeed, in *Total Network SL v. Revenue & Customs*, [2008] 2 W.L.R. 711 (U.K. H.L.), the House of Lords went further, and said explicitly that, as the torts of intentional interference with economic relations and unlawful conduct conspiracy have developed over time, the concept of unlawful conduct has a different meaning in one tort than in the other: see, for example, the speech of Lord Walker of Gestingthorpe at para. 100.

36 It is not necessary that we go that far in this case. However, rather than automatically adopting the meaning of unlawful conduct given in the intentional interference tort cases, I think the better course is to use those cases as a guide, but also consider the kind of conduct that the jurisprudence has found to be unlawful conduct for the purposes of the conspiracy tort.

37 It is clear from that jurisprudence that quasi-criminal conduct, when undertaken in concert, is sufficient to constitute unlawful conduct for the purposes of the conspiracy tort, even though that conduct is not actionable in a private law sense by a third party. The seminal case of *Canada Cement LaFarge* is an example. So too is conduct that is in breach of the *Criminal Code*. These examples of "unlawful conduct" are not actionable in themselves, but they have been held to constitute conduct that is wrongful in law and therefore sufficient to be considered "unlawful conduct" within the meaning of civil conspiracy. There are also many examples of conduct found to be unlawful for the purposes of this tort simply because the conduct is actionable as a matter of private law. In Peter T. Burns & Joost Blom, *Economic Interests in Canadian Tort Law* (Markham: LexisNexis, 2009), the authors say this at p. 167-168:

> There are two distinct categories of conduct that can be described as comprising "unlawful means": conduct amounting to an independent tort or other actionable wrong, and conduct not actionable in itself.
>
> .....
>
> Examples of conspiracies involving tortious conduct include inducing breach of contract, wrongful interference with contractual rights, nuisance, intimidation, and defamation. Of course, a breach of contract itself will support an action in civil conspiracy and, as one Australian court has held, the categories of "unlawful means" are not closed.
>
> The second category of unlawful means is conduct comprising unlawful means not actionable in itself.
>
> .....
>
> The first class of unlawful means not actionable in themselves, but which nevertheless supports a conspiracy action, is breach of a statute which does not grant a private right of action, the very instance rejected in *Lonrho* (1981) by the House of Lords. A common case is a breach of labour relations legislation, and another is the breach of a criminal statute such as the Canadian *Criminal Code*.

38 What is required, therefore, to meet the "unlawful conduct" element of the conspiracy tort is that the defendants engage, in concert, in acts that are wrong in law, whether actionable at private law or not. In the commercial world, even highly competitive activity, provided it is otherwise lawful, does not qualify as "unlawful conduct" for the purposes of this tort.

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39 The appellants submit that while Purina's breach of its contract with Raywalt was sufficient to qualify as "unlawful conduct", neither Ren's nor McGrath did anything that would do so. I agree. In my view, the trial judge used an approach that is too broad. Assessed against the correct test, their conduct was not unlawful.

40 Dealing with Ren's conduct, at the time it purchased feed from McGrath, it had no contract with either Purina or Raywalt. Ren's was free to purchase Purina feed from McGrath at the best price it could obtain and sell it wherever it could. I disagree with the trial judge's conclusion that Ren's was not entitled to be able to obtain Purina feed for resale at advantageous pricing available only to Purina dealers. Ren's conduct in doing so breached no contract. Nor was this conduct tortious or in breach of any statute. Indeed, the trial judge explicitly found that Ren's committed no crime or tort apart from the conspiracy. Ren's required no authorization from Purina to act as it did.

41 On appeal the respondent advanced for the first time the proposition that Ren's induced Purina to breach its contract with Raywalt and induced McGrath to breach its contract with Purina. Neither of these allegations was advanced at trial. They are belied by the trial judge's finding that, other than conspiracy, Ren's committed no tort. Moreover, the trial judge's finding that Purina knew of, and approved of the arrangement between Ren's and McGrath, leaves little room for the conclusion required by the inducing breach of contract tort, namely that Ren's caused Purina to breach its contract with Raywalt or induced McGrath to breach its contract with Purina, assuming such a breach could be found. There was nothing in Ren's conduct that was wrong in law. It was not "unlawful conduct" for the purposes of the tort of conspiracy.

42 Turning to McGrath's conduct, the trial judge found it to be "unlawful" because McGrath had no authority to effectively establish a sub-dealership for Ren's to obtain Purina feed at advantageous prices and then sell it into Raywalt's territory. The trial judge characterized McGraths' conduct as a violation of Purina's standard operating procedures. He therefore did not find McGrath's conduct to constitute a breach of his contract with Purina. Indeed, the standard dealership agreement that Raywalt and Ren's had with Purina did not prohibit such an arrangement. Moreover, the trial judge could not have found McGrath to be in breach of his dealership contract with Purina. His finding that Purina knew and approved of what McGrath was doing precluded that possibility, even if such a prohibition had been a term of McGrath's contract. There is no suggestion that McGrath's actions were tortious or in violation of any statute or in other way wrong in law. In my opinion, McGrath's actions cannot be said to be "unlawful conduct" for the purposes of the tort of conspiracy.

43 In summary, I conclude that only Purina engaged in any unlawful conduct. The other two appellants did not. As a consequence, the finding of unlawful conduct conspiracy and the damages flowing from it must be set aside. The respondents' claim based on civil conspiracy must be dismissed.

Second Issue — The Method of Calculating Breach of Contract Damages

44 In *Hamilton*, Ms. Hamilton entered into a contract with Open Window Bakery Ltd. ("Open Window") for a term of 36 months to serve as its exclusive agent in Japan. The contract gave Open Window the unconditional right to terminate the contract on three months' notice, effective after the commencement of the nineteenth month of the contract. In the sixteenth month, Open Window wrongfully terminated the contract. The trial judge determined Ms. Hamilton's damages by inquiring into how Open Window would likely have performed its obligations under the contract hypothetically, but for its repudiation. This resulted in an award reflecting the payments that would have been made over the full 36 month term less a 25 per cent reduction for contingencies.

45 The Supreme Court held that this was the wrong approach and substituted a damage award based on early termination at the nineteen month mark together with three months' notice, reflecting Open Window's maximum exposure to damages. The court based this on the principle articulated in *Cockburn v. Alexander* (1948), 6 C.B. 791 (Eng. C.P.) that, generally speaking, where there are several ways in which the contract might be performed, the mode that is adopted is the least profitable to the plaintiff and the least burdensome to the defendant, for the purposes of assessing

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damages. The court described the rationale for this principle and the error in the approach used by the trial judge in the following language:

> This tort-like analysis proposed by Hamilton is not an established part of Canadian law. There are compelling reasons for this. Contractual obligations are voluntarily assumed by parties and given effect to by the courts. The failure to perform certain promised positive contractual obligations in contract law is conceptually distinct from the breach of unpromised negative obligations to not harm another's interests in tort law: see G. H. L. Fridman, *The Law of Torts in Canada* (2nd ed. 2002), at p. 11.
>
> In a successful tort claim for damages, unliquidated damages are awarded to a plaintiff on the basis that the plaintiff has suffered a loss through some wrongful interference by the defendant. The plaintiff in such cases has legally protected interests that have been found by a court to be unduly compromised. In tort cases, it is widely recognized that the inquiry into what would have been but for the tort is appropriate, since the plaintiff's interest is in being restored to (or at least awarded compensation in respect of) the position the plaintiff would otherwise be in. See Fridman, *supra*, at p. 2; A. M. Linden, *Canadian Tort Law* (7th ed. 2001), at p. 4, ("[f]irst and foremost, tort law is a compensator"); J. G. Fleming, *The Law of Torts* (9th ed. 1998), at p. 5; and R. F. V. Heuston and R. A. Buckley, *Salmond and Heuston on the Law of Torts* (21st ed. 1996), at pp. 8-9.
>
> However, under the general principle applicable in breach of contracts with alternative performances enunciated above, it is not necessary that the non-breaching party be restored to the position they would likely, as a matter of fact, have been in but for the repudiation. Rather, the non-breaching party is entitled to be restored to the position they would have been in had the contract been performed.
>
> In this case, the relevant contractual duties have been expressly set out by the parties in the agreement. Hamilton is entitled to OWB's performance of these voluntarily assumed duties. Hamilton has no compensable interest in the advantages she might have expected under any particular performance of the contract, since the contract itself provided for alternative methods of performance at the election of the defendant. If Hamilton wanted to secure herself the benefits associated with a given particular method of performance, she should have contracted for only that method of performance.
>
> [Emphasis in original.]

46 The trial judge distinguished *Hamilton*, finding that it applied only where the parties acted honestly and in good faith, and that Purina had not done so, having "conducted itself in a manner that 'defeated or eviscerated the very purpose and objective' of its agreement with Raywalt".

47 With respect, I do not agree. The trial judge erred in finding *Hamilton* to be premised on good faith conduct by the breaching party. Contrary to his view, there was no finding by the trial judge in *Hamilton* that Open Window had acted in good faith at all material times. Nor is there any suggestion in the Supreme Court's decision that good faith conduct is a pre-requisite for the least burdensome principle to apply. Indeed, Open Window had wrongfully terminated Ms. Hamilton by repudiating the entire contract, thereby defeating its very purpose, yet the least burdensome principle of calculating damages was applicable.

48 In my view, *Hamilton* cannot be distinguished as the trial judge did, and should have been followed in assessing the breach of contract damages in this case, even if Purina did not act in good faith in breaching the contract.

49 Had that been done, the trial judge would not have embarked on a hypothetical inquiry into how Purina would likely have performed its obligations under the contract if it had not breached the contract. That is the very sort of inquiry that *Hamilton* says should not be done in approaching breach of contract damages where there are alternate modes of performing the contract.

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50 The contract provided that Purina had the unconditional right to cancel the contract at any time on sixty days' notice. Article V(B) of the contract reads, "Notwithstanding anything to the contrary in this article, either of the parties may cancel this Agreement at any time by giving sixty (60) days advance notice to the other party." There is no doubt that this is the least burdensome mode of performance for Purina. It should have been used as the basis for calculating the damages for breach of contract.

51 Moreover, by finding an implied duty of good faith on Purina not to act in a way that defeats the very purpose of the contract and then finding that Purina could not rely on Article V(B) because it breached that implied duty, the trial judge erred by using the implied duty of good faith to alter the express terms of the contract, including the right to terminate on notice. In *Transamerica Life Canada Inc. v. ING Canada Inc.* (2003), 68 O.R. (3d) 457 (Ont. C.A.), at para. 53 this court made clear that Canadian courts have not accorded this power to an implied duty of good faith.

52 The trial judge also suggested that it would be unconscionable in these circumstances to allow Purina to rely on a clause like V(B) in the calculation of breach of contract damages. I do not agree that unconscionability can be used in this way. In my view, that doctrine is applicable to determine whether the contract itself is unconscionable, given, for example, the circumstances in which it was made. The doctrine is not applicable to determine how damages should be assessed in light of the circumstances of a particular breach.

53 In summary, I conclude that the trial judge erred in failing to apply the approach in *Hamilton* to calculate the damages owed by Purina for its breach of contract. His task should have been to calculate the breach of contract damages needed to restore Raywalt to the position it would have been in had the contract been performed, adopting the mode of performance provided by the contract that is least burdensome to Purina.

54 The trial judge found that had Purina performed the contract, there is no doubt that Raywalt would still have been in business at the end of January 1992, when it in fact closed its doors. At that point, the contract gave Purina the unconditional right of cancelling the agreement on sixty days' notice. This was the mode of performance least burdensome to Purina and therefore constituted its maximum exposure for damages for breach of the contract with Raywalt.

55 Using this approach, the quantification of the damages owed by Purina for breach of contract requires the determination of the amount Raywalt lost because of Purina's breach from the time Raywalt opened for business in March 1991 until the end of March 1992, two months after it actually closed its doors.

56 In my view, the trial judge made findings of fact sufficient for this court to do that calculation, recognizing that this exercise is more of an art than a science. He calculated that, had Purina performed its contractual obligations, Raywalt would have had a profit of $145,654 at the end of January 1992, instead of being insolvent.

57 He arrived at this amount after considering the expert evidence, together with evidence of additional pet food sales that Raywalt would have been able to make in the last two months of that first year of operation. The appellants attack this figure on two bases.

58 First, they say that the expert opinion relied on already included the additional pet food sales and that it was an error to count them a second time. I do not agree. The expert's evidence makes only cryptic reference to the pet food sales and it was entirely open to the trial judge to find that they were not included in the expert's opinion of Raywalt's first year profits and could therefore properly be added to the expert's calculation of loss in the first year.

59 Second, they say that the trial judge did not add to Raywalt's costs the additional costs that would have been required in achieving these additional sales. Again, I disagree. There was an ample evidentiary basis for the trial judge to reach the conclusion he did for both Raywalt's gross sales and its expenses had Purina honoured its contract.

60 I see no basis for interfering with the trial judge's valuation of first year profits lost to Raywalt.

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61 The trial judge also calculated the net profits that Raywalt would have achieved in its second year of operation had the appellants acted lawfully, as part of his calculation of tort damages. He quantified that loss at $318,071. The appellants raise a number of challenges to this calculation, all of which I reject, as explained in the next section of these reasons. I am therefore prepared to accept that figure as the profits Raywalt would have made in its second year of operation had Purina not breached its contract. This provides a good basis for determining the profits lost to Raywalt through February and March 1992, representing the 60 days' notice Purina was required to give, which I would assess at one-sixth of this number, namely $53,011.83.

62 Thus calculated, I would fix the damages to which Raywalt is entitled for Purina's breach of contract at $145,654 plus $53,011.83 for a total of $198,665.83.

Third Issue — The Calculation of Damages

63 As I have indicated, the trial judge concluded that damages for the unlawful conduct conspiracy should reflect the ongoing concern value of Raywalt at the time it was harmed. He calculated this by assessing what the net profit of the business would have been in its second year of operation and then applying a three times earnings multiple to that figure.

64 The appellants raise a number of challenges to his assessment of Raywalt's net profit for that second year. Although I have found that the finding of unlawful conduct conspiracy cannot stand, it is necessary to address these challenges since I have used the calculation of Raywalt's net profits for the second year to calculate Raywalt's contract damages for February and March 1992.

65 First, the appellants say that the trial judge made several errors, resulting in an overvaluation of the contribution that additional pet food sales would have made. They say that the trial judge double counted that contribution by adding it to the expert evidence he relied on. I disagree with this, as I have explained above. They also say that the trial judge impermissibly relied on hearsay evidence in making his finding. I disagree. In my view, it was open to him to rely on the evidence he did hear, which was completely unobjected to at trial by the appellants. Lastly, they say that the trial judge insufficiently discounted for the possibility that these additional sales might not take place. However, the discount to be applied was an assessment that the trial judge was entitled to make on the evidence before him. That is what he did. There is no basis for this court to interfere with it.

66 Second, the appellants argue that the trial judge erred in the discount he applied in using Ren's earnings for the same period as input to calculate what Raywalt would have earned but for the harm inflicted on it. However, the trial judge was fully aware that some discount was appropriate because Ren's sold some products that Raywalt did not. He based the discount he selected on evidence of the percentage of Ren's business that these additional products represented, measured by tonnage. That was a conclusion he was entitled to draw. There is no basis for this court to second guess it and apply a higher discount rate.

67 Third, the appellants quarrel with the trial judge's calculation of the value of Ren's feed sales that Raywalt would have taken over but for the conspiracy. They say that there was evidence of this value that the trial judge should have preferred to the evidence he accepted. In my opinion, that too was up to him. His calculation was based on evidence that he was entitled to act upon. There is no basis for this court to interfere.

68 Fourth, the appellants say that the trial judge committed a palpable and overriding error in assessing the administrative expenses that Raywalt would have incurred in its second year of operation. Again, I disagree. His assessment was well founded on evidence of what those expenses would have been. The trial judge accepted this evidence and made no reversible error in doing so.

69 In summary, I conclude that all of the appellant's challenges to the trial judge's calculation of the profit that Raywalt would have made in its second year of operation must fail.

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Fourth Issue — Pre-Judgment Interest

70 In his original reasons for judgment, the trial judge applied a pre-judgment interest rate of 6.65% to his assessment of damages for breach of contract and unlawful conduct conspiracy. He did so without the parties having an opportunity to make submissions on the issue. He set out his basis for selecting this rate at para. 219 of his original reasons:

> The average rate of interest established for pre-judgment interest by section 128 of the *Courts of Justice Act*, R.S.O. 1990, c. C.43, for 1992, the year in which I find that the cause of action of the plaintiffs arose, is 6.65%.

71 Following the release of these reasons, the trial judge agreed to receive written submissions on the issue. In subsequent reasons, he declined to change the rate he had selected. He gave this explanation at para. 8 of his supplementary reasons:

> More importantly, section 128(1) of the *Courts of Justice Act* shows that the appropriate starting point for the calculation is not the date on which the claim was actually filed, but rather the date on which the cause of action arose: see also *Sedigh v. Lange*, [2000] O.J. No. 3606 (S.C.J.) at para. 11. I focused on when the cause of action arose as the relevant time and found as a fact that the plaintiffs' cause of action arose at some point in 1992 at or about the time that the business failed owing to the actions of the defendants, rather than focusing on the date upon which the plaintiffs filed their claim. As such, I continue to regard it as appropriate to average the quarterly rates for 1992 in the manner that I did at paragraph 219 of my Reasons for Judgment.

72 The appellants also argued at trial that the trial judge ought to have adjusted the rate down to reflect the factors listed on s. 130(2) of the *Courts of Justice Act*. The trial judge concluded his supplementary reasons by rejecting that submission at para. 11:

> Here, the defendants have advanced a range of reasons for their claim that a lower rate should be applicable, but I find that they have done nothing to discharge the onus that rests upon them of persuading me that it is appropriate that I should exercise discretion in this case to deviate from what would otherwise be the applicable interest rate specified by the *Courts of Justice Act*.

73 In this court, the appellants argue that the trial judge erred in this approach.

74 I agree. The pre-judgment rate specified in the *Rules of Civil Procedure* pursuant to the *Courts of Justice Act* for proceedings commenced in the last quarter of 1992, that is, when the respondents' claim was commenced, was 5.1%. That is the applicable rate unless the court finds special circumstances to justify departing from it. In my view, the trial judge erred by taking as his starting point the average pre-judgment interest rate for 1992, the year in which the respondents' cause of action arose, rather than the starting point as specified under the *Courts of Justice Act*. Moreover, he offered no special circumstances for exercising his discretion to deviate from the applicable rate specified by the *Courts of Justice Act*. His error was in using 6.65% as the applicable rate. The proper applicable rate to be used is 5.1%.

Fifth Issue — Punitive Damages

75 Finally, the appellant Purina attacks the award of punitive damages made against it. It argues that the trial judge's basis for doing so did not reach the threshold required by the jurisprudence.

76 In *Fidler v. Sun Life Assurance Co. of Canada*, [2006] 2 S.C.R. 3 (S.C.C.) ("Sun Life"), the Supreme Court of Canada made clear that, in breach of contract cases, conduct warranting punitive damages must be an independently actionable wrong in addition to a breach of contract. As well, it must also reach the threshold warranting punitive damages. The court described that threshold at para. 62:

> By their nature, contract breaches will sometimes give rise to censure. But to attract punitive damages, the impugned conduct must depart markedly from ordinary standards of decency — the exceptional case that can be described

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as malicious, oppressive or high-handed and that offends the court's sense of decency: *Hill v. Church of Scientology of Toronto*, [1995] 2 S.C.R. 1130, at para. 196; *Whiten*, at para. 36. The misconduct must be of a nature as to take it beyond the usual opprobrium that surrounds breaking a contract. As stated in *Whiten*, at para. 36, "punitive damages straddle the frontier between civil law (compensation) and criminal law (punishment)". Criminal law and quasi-criminal regulatory schemes are recognized as the primary vehicles for punishment. It is important that punitive damages be resorted to only in exceptional cases, and with restraint.

77 In coming to his conclusion, the trial judge was clearly influenced by his finding that Purina's conduct was both a breach of contract and part of the unlawful conduct conspiracy. Alternatively, he found that Purina's conduct constituted a second actionable wrong in that it was also a breach of its implied duty of good faith towards Raywalt. Beyond that, he justified the punitive damages award this way at para. 238:

> Here, I find that an award of punitive damages ought to be made against Purina to serve the rational purpose of delivering the simple message that good faith, promises of good faith, and an underlying foundation of business efficacy continue to be what our law relies upon as the cornerstone of upholding and enforcing contractual promises.

78 In my view, this sets too low a bar. It would make every breach of contract that is also a breach of an implied duty of good faith a sufficient basis for the award of punitive damages. I think that would pay insufficient regard to the caution in *Sun Life* that punitive damages are confined to exceptional cases in which the misconduct is of a nature that takes it beyond the usual opprobrium surrounding breaking a contract. It seems to me that breaches of an implied duty of good faith can come in so many possible different shapes and sizes that it cannot be said that generically, the breach of such a duty is *per se* enough to justify punitive damages. It falls, therefore, to this court to determine whether, on the facts as found below, such an award is warranted.

79 In *Sun Life*, the Supreme Court of Canada affirmed that the principles set out in *Whiten v. Pilot Insurance Co.*, [2002] 1 S.C.R. 595 (S.C.C.), at para. 63, continue to govern the award of punitive damages. It reiterated that in breach of contract cases, in addition to the requirement that the conduct constitute a marked departure from ordinary standards of decency, there is the requirement that the acts be "independently actionable". Breach of an implied duty of good faith can satisfy the requirement of an independent actionable wrong: see *Whiten*, at para. 79. The trial judge found that Purina had breached its implied duty of good faith. That was not contested before us and since we received no argument on it we must proceed on that basis. Coupled with breach of the exclusivity contract, the requirement of an independently actionable wrong is therefore met in this case.

80 Thus, the question becomes: did Purina's conduct constitute such a marked departure from the ordinary standards of decency that it warrants censure through the imposition of an award of punitive damages? In answering this question, a careful analysis of Purina's conduct is warranted. In doing so, it is useful to call to mind the factors for consideration set out by the Supreme Court in *Whiten* at para. 94:

> (1) Punitive damages are very much the exception rather than the rule, (2) imposed only if there has been high-handed, malicious, arbitrary or highly reprehensible misconduct that departs to a marked degree from ordinary standards of decent behaviour. (3) Where they are awarded, punitive damages should be assessed in an amount reasonably proportionate to such factors as the harm caused, the degree of the misconduct, the relative vulnerability of the plaintiff and any advantage or profit gained by the defendant, (4) having regard to any other fines or penalties suffered by the defendant for the misconduct in question. (5) Punitive damages are generally given only where the misconduct would otherwise be unpunished or where other penalties are or are likely to be inadequate to achieve the objectives of retribution, deterrence and denunciation. (6) Their purpose is not to compensate the plaintiff, but (7) to give a defendant his or her just desert (retribution), to deter the defendant and others from similar misconduct in the future (deterrence), and to mark the community's collective condemnation (denunciation) of what has happened. (8) Punitive damages are awarded only where compensatory damages, which to some extent are punitive, are insufficient to accomplish these objectives, and (9) they are given in an amount that is no greater than necessary to rationally accomplish their purpose. (10) While normally the state would be the recipient of any fine or penalty for misconduct,

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the plaintiff will keep punitive damages as a "windfall" in addition to compensatory damages. (11) Judges and juries in our system have usually found that moderate awards of punitive damages, which inevitably carry a stigma in the broader community, are generally sufficient.

81 From the outset, Purina knew that in order for Raywalt to succeed, it had to take over Ren's sales of Purina products. As the trial judge found, the volume of Purina sales to Raywalt taken from the Ren's dealership was "critically important" to the success of the new dealership. While the exclusive right to market and sell Purina feed products within defined geographical territories is an important feature of all distributorships, to Purina's knowledge, it was crucial to Raywalt. Further, Purina was aware of the financial risks and vulnerability of Kasemekas and Jackson. As part of the start up financing, Kasemekas gave Purina a mortgage against his home and the company's credit line was secured by personal guarantees by Kasemekas, Jackson and their spouses. The personal guarantees were secured against their homes.

82 It is within this context that Purina's actions must be considered. Within weeks of Raywalt starting up, it learned that Purina was permitting Ren's to continue to supply Ren with feed. When challenged, Purina assured Raywalt that it would stop supplying Ren with feed. While Purina did in fact stop supplying Ren directly, it then embarked on the arrangements with McGrath to ensure that Ren continued to receive feed and sell within the Raywalt territory. That is, in essence, Purina did precisely what it told Raywalt it would not do. It did so repeatedly, over a lengthy period of time and with a complete disregard for the consequences to Raywalt. At para. 49 of the reasons for decision, the trial judge quotes from correspondence authored by Tom Robinson, a manager at Purina, which shows that he had a "clear financial and business interest in McGrath succeeding over Raywalt" and at the relevant times, took an "aggressive stance" against Raywalt. Because of the surreptitious way in which Purina supplied Ren, Raywalk had no knowledge of what was going on and therefore had no ability to take steps to address the problem or mitigate the financial harm that ensued.

83 Purina's actions in supplying McGrath so that he, in turn, could supply Ren are deceitful. As such, they are reprehensible and deserving of sanction.

84 As the preceding reasons explain, the damages award does not otherwise punish this behaviour. There is no "double recovery" aspect to making an award of punitive damages in this case. Moreover, the damages award is insufficient to accomplish the objectives of denunciation and deterrence of others from acting similarly. The amount of $30,000, set by the trial judge is sufficient to do so. Accordingly, I would affirm the punitive damages award, albeit for different reasons than those of the trial judge.

Conclusion

85 In summary, except for punitive damages, I would allow the appeal. I would dismiss the claim of unlawful conduct conspiracy. I would substitute for the damage award for breach of contract an award of $198,665.83, to which I would apply a pre-judgment interest rate of 5.1%. The trial judgment must be amended accordingly, in light of these reasons.

86 This result may be of relevance to the costs awarded at trial and is as well the context for an award of costs of the appeal. The parties may file written submissions of no more than 10 pages on both of these questions within 30 days of the release of these reasons.

E.E Gillese J.A.:

I agree.

R.G. Juriansz J.A.:

I agree.

Appeal allowed in part.

Footnotes

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* Additional reasons at *Agribrands Purina Canada Inc. v. Kasamekas* (2011), 2011 ONCA 581, 2011 CarswellOnt 9210, 86 C.C.L.T. (3d) 206 (Ont. C.A.).

End of Document

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TAB 13

2013 BCCA 352
British Columbia Court of Appeal

XY Inc. v. International Newtech Development Inc.

2013 CarswellBC 2253, 2013 BCCA 352, [2013] B.C.W.L.D. 7022, [2013] B.C.W.L.D. 7032, [2013] B.C.W.L.D. 7050, [2013] B.C.W.L.D. 7114, [2013] B.C.W.L.D. 7155, [2013] B.C.W.L.D. 7214, [2013] B.C.W.L.D. 7260, [2013] B.C.W.L.D. 7261, [2013] B.C.W.L.D. 7263, [2013] B.C.W.L.D. 7266, [2013] B.C.W.L.D. 7267, 115 C.P.R. (4th) 161, 18 B.L.R. (5th) 1, 229 A.C.W.S. (3d) 601, 343 B.C.A.C. 30, 366 D.L.R. (4th) 443, 586 W.A.C. 30

XY, LLC, Respondent (Plaintiff) and Jesse Jia-Bei Zhu, Appellant (Defendant) and JingJing Genetic Inc. (formerly IND Lifetech Inc.), Shu Xi Wang, Selen Zhou, Jin Tang, Respondents (Defendants)

XY, LLC (formerly XY, Inc.), Respondent (Plaintiff) and Selen Zhou, Appellant (Defendant) and Jesse Jia-Bei Zhu, Jin Tang, and JingJing Genetic Inc. (formerly IND Lifetech Inc.), Respondents (Defendants)

XY, LLC, Respondent (Plaintiff) and Jin Tang, Appellant (Defendant)

XY, LLC, Appellant (Plaintiff) and International Newtech Development Incorporated, IND Lifetech Group Ltd., IND Lifetech (U.S.A.) Incorporated, IND Lifetech (USA) Inc., IND Lifetech (Qingdao) Co. Ltd., IND Lifetech (Zouping) Co. Ltd., IND Lifetech (Beijing) Co. Ltd., also known as Beijing IND Embryontech Co. Ltd., IND Lifetech Co. Ltd., IND Embryontech Inc., Shanghai JingJing Biotech Co. Ltd., formerly known as JingJing Genetic (Shanghai) Ltd., IND Lifetech, Inc., now known as JingJing Genetic Inc., Jesse Zhu, Selen Zhou and JinTang, Respondents (Defendants)

Newbury, Chiasson, D. Smith JJ.A.

Heard: May 15-17, 2013
Judgment: July 26, 2013
Docket: Vancouver CA039816, CA038917, CA038918, CA039822

Proceedings: varying *XY Inc. v. International Newtech Development Inc.* (2012), 2012 CarswellBC 663, 2012 BCSC 319, 2 B.L.R. (5th) 19 (B.C. S.C.)

Counsel: R.N. McFee, Q.C., M.D. Shirreff, for Appellant, Jesse Jai-Bei Zhu (CA039816) and, for Appellants, International Newtech Development Incorporated, et al. (CA039822)
J.J. Hunter, Q.C., G. van Ert, for Appellant, Selen Zhou (CA039817)
S.K. Gudmundseth, A.S. Dosangh, for Appellant, Jin Tang (CA039818)
C.S. Wilson, G. Bowman, for Appellant, XY, LLC in CA039822 and Respondent XY, LLC in CA039816, CA038917 and CA039818

Subject: Civil Practice and Procedure; Restitution; Intellectual Property; Contracts; Evidence; Torts; Corporate and Commercial

APPEALS by indivdual defendants from judgments reported at *XY Inc. v. International Newtech Development Inc.* (2012), 2012 CarswellBC 663, 2012 BCSC 319, 2 B.L.R. (5th) 19 (B.C. S.C.), finding defendants liable for torts of deceit and civil conspiracy; CROSS-APPEAL by plaintiff company from judgment finding remaining defendants not liable for damages sustained by plaintiff.

Newbury J.A.:

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1 This matter consists of three appeals and a cross appeal. They arise in the context of a technology licensing agreement between the plaintiff XY, LLC ("XY") as licensor and one of the defendants, JingJing Genetic Inc. ("JingJing"), as licensee. The technology makes it possible to separate X and Y chromosomes in (*inter alia*) bovine spermatozoa, thus permitting the production of calves of a desired sex. The trial judge, Mr. Justice Kelleher, found that JingJing had provided XY with false reports concerning revenues it received from its use of the technology, underpaid the royalties it owed to XY, concealed documents from XY, and violated in several ways the confidentiality provisions in the agreement. JingJing was found liable for breach of contract and the tort of deceit. The award of damages of some $8.6 million against JingJing is not challenged by the plaintiffs; but since the corporation is now bankrupt, the judgment is presumably a dry one.

2 Three of the appeals are brought by individual defendants (the "Personal Defendants") who were employed by JingJing (and by other members of its corporate "group"). The trial judge found that these defendants had committed the torts of deceit and civil conspiracy and awarded the damages jointly and severally against them as well as against their employer. Ms. Jin Tang and Ms. Selen Zhou argue on appeal that they should not have been found liable for JingJing's fraudulent conduct and were simply "following orders". Mr. Jesse Zhu, who was the controlling shareholder of the "IND Group" of corporations and who was clearly the controlling mind of JingJing, cannot make that argument; but he contends the trial judge was wrong to find JingJing had committed the tort of deceit and hence to find that he was a joint tortfeasor with JingJing, or that he committed the tort of civil conspiracy. In his submission, there was no proof that XY had changed its position in reliance on JingJing's misstatements; thus the causation element of the torts was lacking. Finally, Mr. Zhu contends that the trial judge erred in his calculation of the damage award, and challenges as overly broad the terms of a permanent injunction granted against JingJing, the Personal Defendants and "all those over whom they exercise control", in respect of the future use of XY's technology.

3 The plaintiff cross appeals on the basis that other members of the IND Group should also have been found liable with JingJing for the damages suffered by XY. The plaintiff says that like the Personal Defendants, those corporations were joint tortfeasors with JingJing; and that in the alternative they constituted a "common interest entity", so that their individual corporate personalities should be notionally "collapsed" into one with JingJing.

Factual Background

The Parties

4 The trial of these actions occupied 29 days and the facts of the case were described by the trial judge in long and detailed reasons: see 2012 BCSC 319 (B.C. S.C.). I do not intend to try to rehearse them here except as is necessary to explain and determine the points raised on appeal. I begin by attaching as the first schedule to these reasons a copy of the IND corporate "chart" which represents the lines of ownership and control among JingJing and the other IND companies. With one or two exceptions, the chart was in effect at all material times until January 2008. In that month, all the shares of JingJing were transferred to two persons in China, one a friend of Mr. Zhu and the other his brother-in-law. As the trial judge observed, this transaction lacked commercial reality and Mr. Zhu admitted that it had been intended to avoid liability in this proceeding. (Paras. 15 and 118-21.)

5 As the chart indicates, Mr. Zhu at all material times controlled International Newtech Development Inc., ("International Newtech") which in turn controlled JingJing and various other "IND" companies comprising the IND Group. It is worth noting that Excel Advance International Ltd. ("Excel") acquired IND Lifetech Group Ltd. ("IND Cayman") from International Newtech in July 2007. The shares of IND Cayman were later sold to IND DairyTech Ltd., a publicly listed corporation, but Mr. Zhu continued to have effective control through other controlled corporations.

6 The trial judge described the Personal Defendants and their positions in the IND Group as follows:

> The defendant Jesse Jia-Bei Zhu was born in China, and now lives in British Columbia. He is a Canadian citizen. He did his bachelors and masters degrees in China, and originally came to Canada as part of his Ph.D. studies.

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The defendant Richard Remillard is a veterinarian. Mr. Zhu hired him in 2001 as vice president of JingJing. He became president of JingJing in 2003.

The plaintiff discontinued this action against Dr. Remillard as a result of a settlement agreement between them in April 2008.

Under the terms of the agreement, Dr. Remillard agreed to deliver a "comprehensive, true affidavit in response to Interrogatories to be delivered by counsel for the Plaintiff to use in the Proceedings".

The defendant Selen Zhou is the financial manager for IND Embryontech Inc. She did financial management for International Newtech and, until its bankruptcy, JingJing. She also did accounting work for IND (California) and IND (Pennsylvania). She, along with Jesse Zhu, Dr. Remillard and Tang Jin, were the management team of JingJing.

The defendant Tang Jin was the lab manager for International Newtech. She was in charge of embryo production and, later, semen production. [Paras. 28-33.]

7 The plaintiff XY was founded by the Colorado State University Foundation and Cytomation Inc. Until June 2007, Dr. Mervyn Jacobsen was its majority shareholder; since then, it has been controlled by Inguran, LLC, which carries on business as "Sexing Technologies".

The Technology

8 The technology which was the subject of the Commercial License Agreement ("CLA") between XY and JingJing was described as follows by the trial judge:

The plaintiff XY Inc. ("XY") owns technology (and the intellectual property rights associated with the technology) that permits the separation of X (female) and Y (male) chromosomes from bovine spermatozoa. This valuable technology is used as a means of producing calves of a desired sex.

The chromosomes are separated using a cytometer, a device that counts cells. The cytometers that are adapted for this purpose are called SX cytometers. These cytometers are manufactured by DakoCytomation Inc., which has a cross-licensing agreement with XY.

. . .

Thomas Gilligan is a long-time employee of XY and was XY's general manager at the time of the formation of the CLA with JingJing. He served as general manager of XY from 2002 to 2010. He is currently employed by ST [Sexing Technologies].

Mr. Gilligan testified that flow cytometry began some 30 years ago. Scientists in the Silicon Valley studying DNA were doing flow cytometry studies on sperm and realized that X and Y chromosomes could be identified. The United States Department of Agriculture ("USDA") used this knowledge and developed a way of keeping the sperm alive through a sorting process. The USDA acquired a patent and made various improvements to the process.

The first commercial use of this technology was by Mastercalf, a company in the United Kingdom. Mastercalf acquired a license from the USDA to use sorted sperm to create embryos through *in vitro* fertilization or "IVF". IVF is a process of having sperm fertilize oocytes obtained from cows in a fluid medium.

According to Mr. Gilligan, the sorter used by Mastercalf was not fast enough to make the process commercially viable.

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> The next developments were two. First, Colorado State University developed a way to work with more manageable numbers of sperm. Second, a company called Cytomation, Inc., later called DakoCytomation, developed a much faster sorter.
>
> In 1996, XY was formed by the Colorado State University Research Foundation and Cytomation, Inc. Its purpose was to bring this new technology to the marketplace. The first licensee of XY was a company called Cogent in the United Kingdom. Then, XY purchased Mastercalf so XY controlled both "exclusive licenses" that had been issued by the USDA. [At paras. 1-2 and 50-5.]

(Evidently, XY owns or has applied for patents around the world in respect of the technology.)

9 In 1998, Mr. Zhu had established a research laboratory in Canada to carry out the in vitro fertilization ("IVF") of bovine embryos for the Chinese market using Canadian sires. (Para. 56.) In 2003, he, Dr. Remillard and Jin Tang met with XY's CEO, Dr. Jacobsen, to discuss the idea of exporting sexed IVF embryos. The embryos would be exported to China to supply farms that would buy directly from JingJing. After some delays, JingJing and XY agreed on terms that were set out in a letter dated December 26, 2003, and began working towards a more complete arrangement.

10 Progress was delayed by the outbreak of mad cow disease in North America and by China's imposition of a ban on the importation of Canadian embryos. On February 6, 2004, however, XY and JingJing formally entered into the CLA. In general terms, XY agreed to permit JingJing to use its technology during the currency of the Agreement in return for a royalty based on the number of 'sexed' embryos JingJing sold in China, and granted JingJing options to manufacture "AI" (artificial insemination) "straws" containing cattle sperm for sale in China. In return for these licences, JingJing agreed to pay XY an initial fee plus a royalty on gross receipts received from the use or sale of licensed products. It is perhaps unnecessary to add that the CLA contained strict covenants on the part of JingJing designed to preserve the confidentiality of XY's technology.

11 JingJing had to meet certain specified standards before the business terms of the CLA came fully into effect, but after some further amendments to the Agreement (see para. 74 of the reasons) and after purchasing two SX cytometers, JingJing achieved "commercialization" in October 2005.

12 The relationship between the contracting parties was marred by dishonesty on the part of JingJing from the very beginning. The trial judge described at paras. 75-7 and 250, for example, an attempt by JingJing to amend the royalty provisions in the Agreement without XY's consent and in full knowledge that it had not agreed to the amendment. Dr. Jacobsen noticed the change and warned Dr. Remillard that he did not "do business that way". (Para. 76.)

13 Evidently, JingJing was not deterred. It proceeded to violate various terms of the CLA, beginning with its entering into contract-sorting agreements with certain parties in August 2006, conduct that was prohibited by the CLA. (Para. 80.) XY expressed its objections, but JingJing proceeded to breach the Agreement in other ways — by selling sexed semen (not permitted by the terms of the CLA) and representing to XY that it was not doing so; by materially underreporting its embryo production (carried out partly through a veterinary clinic in Abbotsford, British Columbia and partly through other IND subsidiaries in Quebec and the United States) and selling in China; by taking steps to challenge XY's patents in China (prohibited under the CLA); and by attempting to sell SX cytometers to unauthorized parties in China. JingJing lied about or covered up these breaches through the production of false reports to XY which Ms. Zhou and Ms. Tang helped to prepare.

14 Finally, on October 12, 2007, XY commenced its action in British Columbia against JingJing. It obtained an *ex parte* interim injunction restraining JingJing from transferring, selling, licensing, disclosing or in any way disposing of the cytometers or the confidential information that was the subject of the CLA. (See 2007 BCSC 1666 (B.C. S.C.).) Later, other claims and counterclaims were filed by and against other parties, and in August 2008, XY filed its consolidated statement of claim, alleging breach of contract, breach of confidence, deceit, conspiracy, inducing breach of contract, unlawful interference with economic relations, and unjust enrichment against the defendants herein.

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15 There were further dealings between the parties, but XY ultimately terminated the CLA in November 2008. (Para. 141.) In the lead-up to trial, all the counterclaims were either dismissed or withdrawn; and six weeks before the trial date, JingJing filed for bankruptcy.

Material Findings

16 The trial judge made the following findings that are material to these appeals:

• Notwithstanding their arguments to the contrary, the defendants had been given notice of the "live issues at trial via the originating documents" and had not been "prejudiced [in the course of the litigation] in giving their side of the story." (Para. 174.)

• The evidence of each of Jesse Zhu, Jin Tang, and Selen Zhou was largely unsatisfactory and was contradicted by the plaintiff's evidence, including various emails to which the Personal Defendants were party. (Paras. 175-81.)

• JingJing was in an "obvious and substantial breach of contract". Its breaches took the following forms:

  • failure to keep accurate records in accordance with article 3.3 of the CLA;

  • failure to produce accurate records in accordance with article 3.4;

  • failure to report production to XY on a monthly basis in accordance with article 3.1.4;

  • failure to pay royalties monthly in accordance with articles 3.1.1 and 3.1.4;

  • failure to not sub-license the use of XY's technology in accordance with article 2.6;

  • failure to disclose and assign developments made with third parties using XY's technology in accordance with articles 6.2.2 and 6.2.3;

  • failure to maintain the confidentiality of XY's confidential information in accordance with article 3.10. (Paras. 187-8.)

• There had been a "widespread misuse of XY's technology and information amounting to a breach of confidence." These misuses included JingJing's failure to notify XY of research and development related to the technology as required by the CLA; challenges by JingJing to XY's patent applications in China; and the creation of sorting operations in China — all contrary to the CLA. The appropriate remedy for breach of confidence, the trial judge found, would be to grant a permanent injunction. (Para. 229).

• Jesse Zhu, Selen Zhou, and Jin Tang had not induced or procured the breach of contract by JingJing and were therefore not liable for the tort of inducing breach of contract. (This tort had been pleaded but was not addressed in the plaintiff's closing submissions.) In the trial judge's words, the Personal Defendants "did not induce JingJing to breach his contract with XY. Rather they were <u>carrying out</u> JingJing's breach of contract." (Para. 235; my emphasis.)

• The Personal Defendants and JingJing were "joint tortfeasors in deceit" (para. 262) and in the alternative, were liable for the tort of conspiracy by unlawful means. (Para. 277.)

• The evidence did not establish that the tort of deceit committed by the Personal Defendants was committed "in concert with the corporate members of the IND Group (beyond JingJing), or that it was committed on their behalf." (Para. 298.)

• The trial judge assessed XY's damages at paras. 278-96 of his reasons. Since JingJing had failed to produce records that would show how many embryos it had used in China, the trial judge had to do his best to assess this quantity

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and to assess their fair market value before and after January 2007, when the IND Group began using sexed semen from "proven sires". The trial judge calculated XY's damages as follows:

1	IVF embryos before January 2007: 500,000 embryos × 10% of $125 f.m.v.		6,250,000
2	IVF embryos after January 2007: 100,000 embryos × 10% of $150 f.m.v. (This does not include post December 2008 — this will be referred to the Registrar)		1,500,000
3	*In vivo* embryos: 1,147 embryos × 20% of $350 f.m.v.		80,290
4	Semen production: 195,148 AI straws × $6 royalty		1,170,888
5	LESS: Royalties already paid		(20,616)
6	LESS: Summary judgment paid		(472,671)
		TOTAL:	$8,507,891

As I understand it, this award represents the Court's best assessment of the royalties that JingJing should have paid and would have paid it had it accurately reported its revenues as required by the CLA, less the royalties it had remitted — i.e., the amount necessary to place XY in the position it would have been if JingJing had performed its obligations under the CLA.

• The trial judge declined to disregard the separate legal identity of the various IND corporations, observing that Canadian courts take a "restrained" approach to piercing corporate veils. He saw "no legal basis for the Court to disregard the juristic personhood of each individual member of the IND Group". Further, he stated:

> The plaintiff's complaint is that JingJing sold or transferred its products to IND companies which did not pay it. When JingJing became bankrupt, XY had no recourse against it.
>
> I agree with the defendants, however, that the IND group of companies are not liable. The fact that Mr. Zhu treated them as a "common interest entity" does not entitle the court to disregard their separate legal personality as corporations. The circumstances of this case and of the corporate members of the IND Group do not rise to a level where the consequences of the individual defendants' torts or those of JingJing's breach of contract should flow throughout the IND Group to its individual members.
>
> The plaintiff's contract was with JingJing. None of the corporate defendants is party to the CLA. In the absence of a piercing of the corporate veil, or a finding of tortious activity on the part of one of the corporate defendants, there is no basis for liability. [At paras. 316-18; emphasis added.]

• With respect to unjust enrichment (which was argued in XY's submissions in reply at trial), the trial judge concluded that given his findings on the other torts, it was not necessary to carry out an analysis of this doctrine. (Para. 320.) However, he also stated:

> Insofar as the claim may apply to the other corporate IND defendants which have thus far not been found liable, there is a paucity of evidence showing the manner in which other members of the IND Group have been enriched. The plaintiff's loss and the lack of juristic reason for any resulting enrichment have been established but, without more, the claim in unjust enrichment against the other corporate defendants in the IND Group must fail. [At para. 321; emphasis added.]

• XY was entitled to a permanent injunction in the terms proposed by the plaintiff. Attached to these reasons as Schedule II is a copy of the relevant paragraphs of his order imposing the injunction, and Appendix A referred to therein.

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- The trial judge declined to award punitive damages (para. 348), but awarded special costs against JingJing and the Personal Defendants in light of their attempts to mislead the Court during the litigation process, their untruthfulness in giving evidence at trial, and their failure to disclose documents. (Para. 361.)

Damages

17 As mentioned, the damages award was apparently an assessment of what amount would put XY in the position it would have been in if JingJing had properly performed its obligations with respect to the payment of royalties under the CLA. This of course is the measure of damages in contract. Mr. Wilson, counsel for the plaintiff, had advised the Court that his client was prepared to limit its damage claim to lost royalties, and thus presumably to forego compensation for other losses (including the diminution in the value of the technology) which would have been more difficult and costly to prove. The injunctive relief sought by XY was intended to protect against, or minimize, such losses in future.

18 In these circumstances, it seems to me that if one were to calculate damages on a "reliance" basis, i.e., as the measure of what amount would be necessary to place XY in the position it would have been if no misrepresentation had occurred (see *BG Checo International Ltd. v. British Columbia Hydro & Power Authority*, [1993] 1 S.C.R. 12 (S.C.C.), at 37), the amount would likely be the same or close to the same. As will be seen below, Canadian courts in considering tort claims that arise in the contractual context seem to be willing to assume that if no misrepresentation had occurred, the defendant would have provided accurate statements and paid the plaintiff what it owed under the contract. (See especially *3Com Corp. v. Zorin International Corp.* (2006), 211 O.A.C. 222 (Ont. C.A.) at para. 57; and *Wiebe v. Gunderson*, 2004 BCCA 456 (B.C. C.A.) at paras. 29-40.)

The Tort of Deceit

19 The trial judge analyzed the evidence with respect to the elements of the tort of deceit beginning at para. 237 of his reasons. Relying on *Han v. Cho*, 2009 BCSC 458 (B.C. S.C.) and *Soleil Hospitality Inc. v. Louie*, 2010 BCSC 1183 (B.C. S.C.), he stated:

> The tort of deceit, also known as civil fraud, is concerned with the intentional inducement of another person to rely upon a representation that the representor knows to be untrue. The elements that make up this tort are:
>
> (1) a false representation of fact by the defendant;
>
> (2) made with knowledge of its falsity or recklessly, ie. not caring whether it is true or not;
>
> (3) made with the intention that the plaintiff would act on it;
>
> (4) with the intention that the plaintiff would act on it; and
>
> (5) the plaintiff suffered damages. [At para. 237; emphasis added.]

20 The judge referred to certain textbook discussions of deceit which had been cited by this court in *Catalyst Pulp & Paper Sales Inc. v. Universal Paper Export Co.*, 2009 BCCA 307 (B.C. C.A.). He noted in particular a passage from Professor G.H.L. Fridman's text, *The Law of Torts in Canada* (2nd ed., 2002):

> Before a defendant can be liable for deceit it must be established, as a matter of fact, that the plaintiff relied on the defendant's misrepresentation. Such reliance was proved to have occurred in *Dixon v. Deacon Morgan McEwan Easson* [(1993) 102 D.L.R. (4th) 1 (B.C.C.A.)] where the plaintiff purchased the shares as a result of reading the press release containing the inaccurate financial statements about the company.
>
> Although in general it is for the plaintiff to prove the requisite reliance, it would seem that once the plaintiff establishes that the defendant made a misrepresentation calculated to induce the plaintiff to act to his detriment

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and loss consistent with the plaintiff's having acted on the misrepresentation, the onus then shifts to the defendant to prove that the plaintiff did not in fact rely on the misrepresentation in issue. [At 750-1.]

21 The judge then considered each of the elements of the tort he had listed in his para. 237, finding that the defendants JingJing, Mr. Zhu, Ms. Zhou and Ms. Tang had knowingly made false representations to XY at least until 2008; and that they had intended for XY to rely on those representations. Then, with respect to the last two elements he stated:

The Plaintiff's Reliance

Finally, the plaintiff did act on it. Until the true facts were discovered, the plaintiff had no way of knowing it was receiving less than what it was owed, and that it was therefore entitled to recover damages.

Damages

There is no serious issue about the fifth element of the tort of deceit: the plaintiff undoubtedly suffered damages. [Paras. 260-61; emphasis added.]

Analysis

22 Both Mr. Hunter on behalf of Ms. Zhou and Mr. McFee on behalf of Mr. Zhu took issue with the trial judge's statement of the elements of the tort of deceit, and with his conclusion that the tort was proven in this case. First, counsel submitted that the fourth and fifth elements stated by the trial judge at his para. 237 were incorrect or incomplete: the fourth element was obviously a repetition of the third, and the final element did not capture the requirement of causation — i.e., that the plaintiff must have suffered damages *as a result* of its reliance on the false statement.

23 Many authors combine the fourth and fifth elements described by the trial judge into one, so that the following four elements as stated in *Peek v. Derry* (1889), L.R. 14 App. Cas. 337 (U.K. H.L.) are generally said to be the following:

1) a false representation or statement made by the defendant,

2) the statement was knowingly false,

3) the statement was made with the intention to deceive the plaintiff, and

4) the statement materially induced the plaintiff to act, resulting in damage.

(See also Lewis N. Klar, *Tort Law* (2nd ed. 1996) at 490 and Fridman, *supra*, at 747-55.)

24 In Spencer Bower, Turner and Handley, *Actionable Misrepresentation* (4th ed., 2000), the authors break down the four requirements into eight in the following passage:

An action for damages for fraudulent misrepresentation at common law was an action for deceit. The Court of Chancery exercised a concurrent jurisdiction with the Courts of Law in cases of actual fraud, and could award equitable compensation on similar, but not identical, principles, and also specific relief. In either case a representee must allege and prove:

1) a representation;

2) that the defendant was the representor;

3) that the plaintiff was a representee;

4) inducement;

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> 5) falsity;
>
> 6) alteration of position;
>
> 7) fraud;
>
> 8) damage.
>
> The first six matters are common to all claims for misrepresentation ... The seventh and eighth, fraud and damage, are peculiar to actions in deceit.
>
> From the earliest times it has been recognized that the concurrence of fraud and damage is essential to a claim for damages for fraudulent misrepresentation. [At §181-2; footnotes omitted; emphasis added.]

The authors also state that the representee must establish that "he was induced not just to believe [the misrepresentation] but to *alter his position* in a manner affecting his interests" (at §138). They continue:

> 140 Entry into a contract with the representor or a third person is the most common alteration of position. But there are other transactions involving economic loss, present or contingent, which the representee may be induced to undertake which constitute an alteration in position. They include unilateral acts such as payments, gifts, licences and consents, condonations of matrimonial offences, forbearances, and renunciations, and acts which render the representee civilly responsible to some third person, or in breach of the criminal law, which would not have done so if the statement had been true.
>
> [Emphasis added.]

25 Similarly, the editors of *Halsbury's Laws of England* (4th ed.) state that the representee must "establish that he was induced by [the misrepresentation], *not merely to alter his mind, but to alter his position, that is to say, to effect a change in his material or temporal interests or situation.*" (Vol. 31 at §778; my emphasis.) The editors continue:

> There are various ways in which a representee may act on the faith of a representation so as to alter his position. He may enter into a contract either with the risk of representor himself, or with a third person, or class of persons, or the alteration of position may take the form a unilateral transaction of a binding nature, in the sense that it is not revocable except with the consent of the other party to it, such as a gift, licence or consent, a forbearance or a renunciation, or it may consist in an act, of whatever nature, the effect of which is to render the representee civilly responsible to some third person, or even to render him amenable to criminal process, if such act would not have constituted any offence at all if the statement on the faith of which he committed it had been true. Further, a person may physically alter his position by the act of using property, whether land or a chattel, in reliance on a representation ... and, generally, by the doing of or abstention from anything which has a bearing on his material interests, and which he is not legally compellable to do or to abstain from. [At Vol. 31, §779; emphasis added.]

26 The Personal Defendants rely on these textbook formulations of the tort of deceit, arguing that XY did not change its position in reliance on the false statements made to it by JingJing or any other defendant. Instead, XY simply carried on with the performance of its obligations under the contract, as it would have if JingJing's statements had been true. Thus while the plaintiff suffered damages in contract, these defendants contend it did not prove damages flowing from an act of the plaintiff carried out in reliance on JingJing's false statements.

27 Mr. Wilson on behalf of XY emphasized that the texts uniformly cite "forbearance" as a type of alteration of position. In support, the authors cite only *Firbank's Executors v. Humphreys* (1886), 18 Q.B.D. 54 (Eng. C.A.). In *Firbank's*, a railway company that was indebted to a contractor purported to give him certificates for debenture stock in return for the contractor's forbearing from pressing the railway for payment and finishing the railway line. Later, when the railway was wound up, it was discovered that it had already issued the whole of its debenture stock and that the

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certificates given to the contractor were worthless. The contractor sued the directors of the railway company personally for the value of the debentures as if they had been validly issued.

28 Lindley, L.J. formulated the two questions before the Court in *Firbank's* as "(1) Whether the directors are to be treated as having impliedly warranted that they, as agents of the company, had authority to issue 18,400£ debenture stock? (2) What is the measure of damages for which they are liable if they are to be so treated?" He answered the first question in the contractor's favour, even though the directors had not known they had lacked the authority to issue the debentures. With respect to the second question, Lindley L.J. wrote:

> The directors cannot be treated as having warranted the solvency of the company, and if genuine debenture stock of the company had been worthless, the measure of damages would have been nil, but in this case the company's debenture stock is and always has been worth twenty shillings in the pound. Consequently, the value of 18,400£ genuine debenture stock is the measure of the contractor's loss. That is what he agreed to take in satisfaction of a larger demand, and that is what he has lost by reason of the misrepresentation made to him. [At 62-3.]

The Court did not elaborate on forbearance or change of position generally.

29 There appear to be only a few modern Canadian cases that address situations in which the parties entered into a contract *prior to* the making of the false statements. One is *Catalyst Paper, supra*. Like this case, *Catalyst Paper* involved an ongoing contract that called for regular reports and invoices, although in this instance, the payments were to be made *by* the plaintiff "Catalyst" *to* the defendant "UPE". UPE had been engaged by Catalyst to facilitate the delivery and distribution of telephone directory paper to an Australian customer. Under the contract, UPE regularly invoiced Catalyst for certain costs, but the parties were not *ad idem* as to whether UPE was entitled by the terms of the contract to "mark up" certain distribution costs it incurred in Australia. Catalyst assumed that UPE was passing on only its actual costs and paid UPE's invoices from time to time. When it discovered the costs had been marked up, it sued in contract, breach of fiduciary duty, unjust enrichment, and fraudulent misrepresentation.

30 Catalyst's claim in contract failed because, in the trial judge's words, "there was no explicit agreement at the stage of the formation of the contract that the figures used would reflect actual costs." For the same reason, the claim in unjust enrichment also failed: it "could not be said there existed no juristic reason to compute the sales price from Catalyst to UPE by discounting the specified amounts agreed on by the parties from time to time during the course of the [agreement]." (Paras. 44-5.)

31 Catalyst succeeded, however, in its claim for deceit, both at the trial level and on appeal. In the Court of Appeal, UPE submitted that the law of fraudulent misrepresentation required proof that Catalyst had been induced to enter its contract with UPE by the misrepresentation. On this point, UPE relied on G.H.L. Fridman, *Law of Contract in Canada* (4th ed. 1999) at 309-10, where the author listed four elements of deceit, the last of which was that the victim "must have been induced by the representation to enter into the contract." Bauman J.A. (as he then was) for this court noted however that the author himself took a wider view of the "reliance element" of the tort in *The Law of Torts in Canada, supra*. [At 750-1: see above at para. 20.]

32 In *Catalyst Paper*, the trial judge found that the defendant had intended that the plaintiff "act on the representation by *not focusing on, inquiring into, or assessing the appropriateness of the amount paid to Chase [a facilitator for UPE in Australia]*." (My emphasis.) The Court of Appeal's treatment of reliance was more equivocal:

> It is implicit, if not express, that the trial judge found that the false representations began with the cost information forwarded by UPE from the beginning of its relationship with Catalyst in July 1999, September 1999, November 1999, February 2000, and regularly throughout the currency of the PSA. If an actual inducement to enter into the contract is required, the false representations in the Fall of 1999, and in February 2000, so induced Catalyst. And it is beyond doubt, as the trial judge found, that the false representations continued to induce Catalyst to alter its position to its detriment throughout the course of the arrangement with UPE. I note particularly the costing

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> information sent to Catalyst at regular intervals during the PSA "for its approval"; an approval obtained, again, on the basis of the false representation that UPE passed along only actual costs and that those of Chase were subsumed in the 3% commission paid to UPE.
>
> In my view, the case against UPE for fraudulent misrepresentation was overwhelming. The judge committed no reversible error of law or fact in his disposition of the matter on this basis. [At paras. 62-3; emphasis added.]

33 The Court in *Catalyst Paper* also referred to *Kelemen v. El-Homeira*, 1999 ABCA 315, 250 A.R. 67 (Alta. C.A.), in which a vendor of real estate had persuaded a prospective purchaser not to seek independent advice and instead directed him to one of his colleagues. As a result, the purchaser paid an inflated price for the property. The Court stated that "The action taken by [the plaintiff] that is the basis for the tort was that *he did not seek the independent advice*". (Para. 15; my emphasis.) However, the plaintiff also altered his position by entering into the purchase agreement on the basis of the vendor's trickery.

34 The decision of the Ontario Court of Appeal in *3Com Corp. v. Zorin International Corp.*, *supra*, is also somewhat analogous. The plaintiff, "3Com", an electronics manufacturer, entered into an ongoing contract for the sale of goods to a reseller, "Zorin". Zorin represented to the plaintiff that it was reselling the goods to foreign educational institutions, which allowed Zorin to purchase at a discounted rate by claiming rebates that were then paid out by 3Com. In fact, Zorin was selling to purchasers who did not qualify for the rebates. The plaintiff eventually learned of the misrepresentation and sued successfully in deceit. The trial judge found that 3Com had "relied on Zorin's false representations in approving the transactions for ... discounted prices."

35 The Court of Appeal upheld the trial court, rejecting Zorin's argument that in tort, only actual "losses" are to be compensated. In the analysis of Weiler J.A. for the Court:

> I agree with the trial judge's rejection of the appellants' arguments. The appellants' first argument on damages overlooks the fact that, in tort law, "the plaintiff is to be put in the position it would have been in had the misrepresentation not been made": see *BG Checo International Ltd. v. British Columbia Hydro and Power Authority*, [1993] 1 S.C.R. 12 at 37. Although not written into the contracts, a vital condition to their formation was that the appellants deliver the goods to the persons to whom, and the places where, they said they were shipping the goods. The appellants were aware that the purchase price was based on the information they provided as to educational end-user and place. The fact that we are dealing here with a diminution in profit rather than an actual loss matters not. If the appellants had provided the respondents with the true customers and places of shipment, the respondents would have been entitled to a higher price for their goods or to refuse to sell their goods at the prices they did. The appellants deprived the respondents of this choice and made a greater profit because they did so. It was not necessary, in the circumstances of this case, to introduce evidence of a specific alternative third party buyer ... [At para. 57; emphasis added.]

36 It is clear on the facts that 3Com shipped product to Zorin from time to time (see paras. 8 and 44) on the strength of Zorin's false statements and paid the rebates claimed by a fraudulent distributor, thus "altering" not only its "mind", but also its position. As seen above, however, the Court of Appeal did not rely on these acts to satisfy the elements of reliance and causation — although it is unclear whether these elements were squarely addressed in argument. Instead the Court seemed to agree with the trial judge that by 'receiving' lower payments for its goods than what it should have received under the contract, 3Com had relied on the false statements to its detriment. As well, the Court emphasized that the plaintiff would not have entered the contract unless Zorin had obliged itself to deliver the goods to the persons to whom it said it was delivering them. On one view, then, the fact the plaintiff had (*prior to* the misstatements) entered the contract with the defendant constituted an act in reliance on the (*later*) misstatements sufficient to found the tort of deceit. If this is correct, the tort of deceit seems indistinguishable from breach of contract in cases where the deceit is part of an ongoing contractual relationship.

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37 Returning to the case at bar, counsel for the Personal Defendants argued that the trial judge had "conflated" tort and contract by awarding damages without proof that the plaintiff had relied on the misrepresentations. XY submitted in response that the defendants' position was "too categorical." In XY's submission:

> It overlooks the fundamental tort law principle that the plaintiff is to be placed in the same position as it would have been in had the tort not been committed: see *Krangle (Guardian ad litem of) v. Briscoe*, [2002] 1 S.C.R. 205, 2002 SCC 9, at para. 22; and *Ratych v. Bloomer*, [1990] 1 S.C.R. 940, at p. 962, following *Andrews v. Grand & Toy Alberta Ltd.*, [1978] 2 S.C.R. 229.
>
> In cases involving misrepresentations (whether negligent or fraudulent), that first principle translates into an inquiry into the position that the plaintiff would have been in had the misrepresentations not been made: see *BG Checo International Ltd. v. British Columbia Hydro and Power Authority*, [1993] 1 S.C.R. 12, at p. 37.
>
> That inquiry, in turn, often reduces to a determination about the steps taken by the plaintiff in reliance upon the misrepresentation that was made. For instance, where the plaintiff was induced to enter into a transaction on the basis of the misrepresentation, the loss suffered by the plaintiff is the loss resulting from the plaintiff's participation in the transaction — in other words, the reliance measure. *BG Checo* was itself such a case; see also *Wiebe v. Gunderson*, 2004 BCCA 456, 243 D.L.R. (4th) 1 (deceit inducing plaintiff to purchase ranch).
>
> However, where the misrepresentation operates during the performance of an *existing* contractual relationship, the reliance measure may be less apposite to the assessment of damages than when the misrepresentation induces the making of the contract in the first place. This court's decision in *Catalyst Pulp and Paper Sales Inc. v. Universal Paper Export Co.* ... illustrates the distinction.
>
> [Emphasis added.]

38 In addition to *Catalyst Paper*, Mr. Wilson referred us *Rowlett v. Karas* (1943), [1944] S.C.R. 1 (S.C.C.), where the Court stated:

> The *injuria* here was intended to and did bring about a fraudulent termination of the lease and loss of the business. The damages from the deceit are, therefore, the same as the consequences of a breach of the obligations from which the rights and interests of the plaintiff arose; and they are to be determined on the rules applicable to contractual defaults.
>
> It is well settled that the person who has suffered from such a wrong is entitled, so far as money can do it, to be placed in as good a position as if the contract had been performed. [At 7; emphasis added.]

See also *V.K. Mason Construction Ltd. v. Bank of Nova Scotia*, [1985] 1 S.C.R. 271 (S.C.C.), and this court's decision in *Wiebe v. Gunderson, supra*. In the latter, we noted that in cases of fraud inducing a plaintiff to enter into a contract, the trend in Canada and elsewhere is to de-emphasize one particular "measure" of damages and to:

> ... strive for an award that in broad and practical terms compensates the plaintiff for all aspects of his or her loss flowing from the fraud, without being overly restricted by the nature of the cause of action. The overarching question is what amount of money represents the financial loss suffered by the plaintiff as a direct result of the altercation of his or her position under the inducement of the defendant's fraudulent representations. [At para. 40.]

(See also *BG Checo International Ltd. v. British Columbia Hydro & Power Authority*, [1993] 1 S.C.R. 12 (S.C.C.), at 37-42.)

39 It is not the measure of damages with which we are concerned at this stage, however. Rather it is the question of whether the final element of the tort of deceit was proven against the Personal Defendants — assuming for the moment they were not shielded from liability by their employment relationship with JingJing. Here, it cannot be said that as in *Catalyst Paper*, the parties' agreement was entered into in reliance on JingJing's false representations (which obviously

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followed the CLA in time). Nor did XY, like the plaintiffs in *Catalyst Paper* and *3Com*, make payments on the strength of the false statements. It made no conscious decision, as the plaintiff did in *Firbank's*, to forebear from enforcing its rights or to delay taking legal action. In short, it conducted itself in the same way it would have if JingJing's reports had been true. Of course, had it realized the reports were false, the plaintiff might have sued immediately, and succeeded in obtaining its judgment before JingJing declared bankruptcy. But can it be said that XY's carrying on under the contract until it discovered the fraud constituted an act of reliance on its part?

40 To answer this question in the affirmative would be a significant step in the law of deceit. I am reluctant to take such a step on the basis of authorities in which the point was not clearly raised, expressly considered or satisfactorily analyzed. At the same time, I recognize that the law of private obligations in Canada is moving away from a stringent view of causation in tort and from a "categorical" approach to civil causes of action generally: see *BG Checo International Ltd. v. British Columbia Hydro & Power Authority*, *supra.*, at 348 and 41; *Rainbow Industrial Caterers Ltd. v. Canadian National Railway* (1990), 67 D.L.R. (4th) 348 (B.C. C.A.), at paras. 184-5; *Morrison v. Pankratz* (1995), 122 D.L.R. (4th) 352 (B.C. C.A.) at para. 45. See also the discussion by M.J. Tilbury in Two Models of Concurrent Tort/Contract Liability & Their Application to Remoteness and the Measure of Damages in J. Berryman, ed., *Remedies: Issues & Perspectives* (1991) at 423 *et seq.*

41 The Supreme Court of Canada may well wish to provide guidance in this area. On balance, however, I propose to adopt the less stringent view of reliance exemplified by this court's decision in *Catalyst Paper*, by which I am bound, and to accept that in the final analysis, the object is to compensate XY for the losses it suffered by reason of JingJing's fraudulent conduct. I will therefore proceed on the basis that XY's "acceptance" of the payments made by JingJing on the basis of the false reports constituted "reliance" for purposes of the tort of deceit. At the same time, I will consider the defendants' challenges to the trial judge's findings of liability independent of deceit so that if I am wrong regarding that tort, the parties will have a complete case for purposes of any further appeal.

Joint Torts

42 Obviously, the trial judge's finding that the Personal Defendants were joint tortfeasors with JingJing would fall if deceit on JingJing's part were not proven. Conversely, I see no error in the conclusion that if deceit was proven, the Personal Defendants "each played a part and acted in concert to deceive XY ..." (at para. 258, citing *"Koursk" (The), Re*, [1924] P. 140 (Eng. C.A.)), and were therefore jointly liable in tort. (Again, this assumes for the moment that these defendants were not shielded from liability by reason of their employment status.) If this is correct it would be unnecessary to consider the tort of civil conspiracy, which would "add nothing" and could be struck out or "merged". (See *Bank of Montreal v. Tortora*, 2010 BCCA 139 (B.C. C.A.); *Soleil Hospitality Inc. v. Louie*, 2011 BCCA 305 (B.C. C.A.).) In any event, there is very little difference apparent between being a joint tortfeasor in the sense of participating in a "concerted action between [the tortfeasors] to a common end" (see Glanville Williams, *Joint Torts and Contributory Negligence* (1951) at 1), and being a civil co-conspirator.

Civil Conspiracy

Elements of the Tort

43 The elements of civil conspiracy are well settled in Canada, although cases in which liability is found are rare, and the cause of the action is regarded as somewhat "anomalous". (See the seminal decision of Lord Diplock in *Lonrho Ltd. v. Shell Petroleum Co.* (1981), [1982] A.C. 173 (U.K. H.L.).) In the leading Canadian case, *Canada Cement LaFarge Ltd. v. British Columbia Lightweight Aggregate Ltd.*, [1983] 1 S.C.R. 452 (S.C.C.), Estey J. for the Court stated that the tort arises in two possible situations, namely where:

> (1) whether the means used by the defendants are lawful or unlawful, the predominant purpose of the defendants' conduct is to cause injury to the plaintiff; or,

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> (2) where the conduct of the defendants is unlawful, the conduct is directed towards the plaintiff (alone or together with others), and the defendants should know in the circumstances that injury to the plaintiff is likely to and does result. [At 471-72.]

44 The trial judge correctly identified the second branch ("unlawful act conspiracy") as relevant to this case (para. 267) and found that an agreement had existed between Dr. Remillard and the three Personal Defendants. (Para. 270.) In this regard, he identified "concerted action pursuant to the agreement", including "falsely reporting to XY and concealing material documents." (Para. 271.) Next, having found that the Personal Defendants had perpetrated the deceit found earlier in his reasons, the trial judge found that each of them knew or ought to have known that injury to the plaintiff was likely (citing *Golden Capital Securities Ltd. v. Holmes*, 2004 BCCA 565 (B.C. C.A.) at para. 74). Finally, he stated:

> ... I find that the plaintiff suffered a financial loss as a result of the unlawful conduct by the defendants. It was deprived of the royalties to which it was entitled.
>
> For these reasons I concluded that the plaintiff has proved conspiracy on the part of Jesse Zhu, Selen Zhou and Tang Jin. [At paras. 276-7.]

He did not suggest that the amount of these damages should be different from the amount for which JingJing itself was found liable.

45 On behalf of Mr. Zhu, Mr. McPhee submitted in this court that in considering the question of causation flowing from the alleged conspiracy, the trial judge again "conflated" the loss suffered by XY as a result of JingJing's breach of contract, with that flowing from the conduct of the three Personal Defendants. As I understand it, this argument, like that made concerning deceit, turns on the question of causation.

46 I certainly agree that the acts of the defendants must be causally related to loss or damage to the plaintiff for purposes of establishing a civil conspiracy. As stated in *Lombardo v. Caiazzo* (2006), 211 O.A.C. 270 (Ont. C.A.), "A conspiracy that does not result in damages is not actionable." (Para. 16.) The fact that the plaintiff must have suffered loss as a result of the conspiracy, however, does not mean it must have changed its position or relied to its detriment on misconduct of the defendant. In *Canada Cement LaFarge*, for example, the defendants were alleged to have conspired to drive the plaintiff aggregate manufacturer out of business through marketing arrangements aimed at dividing the concrete products market in British Columbia between two of the defendants. Although the plaintiff's claim ultimately failed, no issue arose concerning the sustainability in theory of the plaintiff's claim to loss of the "benefits of a free market" as a result of the alleged conspiracy.

47 A more recent example is *Soleil Hospitality Inc. v. Louie*, 2010 BCSC 1183 (B.C. S.C.), *aff'd* 2011 BCCA 305 (B.C. C.A.), where the defendants conspired to impugn a valid settlement agreement on the basis of rights allegedly arising under non-existent agreements. There was no reliance by the plaintiffs on the false agreements, but the conspiracy was found to be made out.

48 If the tort of deceit were not made out in the case at bar, then, it would not follow that the tort of civil conspiracy on the part of the defendants other than JingJing would also be precluded. As stated above, the causation element of this branch of conspiracy requires only that the plaintiff have suffered "actual damage" as a result of unlawful conduct directed towards the plaintiff.

Unlawful Act

49 There is not a great deal of case law in Canada on the meaning of "unlawful means" or "unlawful act" in the context of civil conspiracy. In 1961, in *Gagnon v. Foundation Maritime Ltd.*, [1961] S.C.R. 435 (S.C.C.), the Court referred in this context to "means ... [that] were prohibited, and this of itself supplies the ingredient necessary to change a lawful agreement which would not give rise to a cause of action into a tortious conspiracy ...". (At 446.) More recently, the

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Ontario Court of Appeal considered the issue in *Agribrands Purina Canada Inc. v. Kasamekas*, 2011 ONCA 460 (Ont. C.A.) in connection with a claim of intentional inference with economic relations. The Court referred to *Bank of Montreal v. Tortora*, *supra*, in which it was said at para. 47 that for conspiracy to lie, the plaintiff must show unlawful conduct by each conspirator. After considering the specific context of intentional interference cases, the Court in *Agribrands* continued:

> [R]ather than automatically adopting the meaning of unlawful conduct given in the intentional interference tort cases, I think the better course is to use those cases as a guide, but also consider the kind of conduct that the jurisprudence has found to be unlawful conduct for the purposes of the conspiracy tort.
>
> It is clear from that jurisprudence that quasi-criminal conduct, when undertaken in concert, is sufficient to constitute unlawful conduct for the purposes of the conspiracy tort, even though that conduct is not actionable in a private law sense by a third party. The seminal case of *Canada Cement LaFarge* is an example. So too is conduct that is in breach of the *Criminal Code*. These examples of "unlawful conduct" are not actionable in themselves, but they have been held to constitute conduct that is wrongful in law and therefore sufficient to be considered "unlawful conduct" within the meaning of civil conspiracy. There are also many examples of conduct found to be unlawful for the purposes of this tort <u>simply because the conduct is actionable as a matter of private law</u>. In Peter T. Burns & Joost Blom, *Economic Interests in Canadian Tort Law* ..., the authors say this at p. 167-168:
>
> > ... Examples of conspiracies involving tortious conduct include inducing breach of contract, wrongful interference with contractual rights, nuisance, intimidation, and defamation. <u>Of course, a breach of contract itself will support an action in civil conspiracy and, as one Australian court has held, the categories of "unlawful means" are not closed</u>.
> >
> > The second category of unlawful means is conduct comprising unlawful means not actionable in itself.
> >
> > . . .
>
> What is required, therefore, to meet the "unlawful conduct" element of the conspiracy tort is that the defendants engage, in concert, in acts that are <u>wrong in law, whether actionable at private law or not</u>. In the commercial world, even highly competitive activity, provided it is otherwise lawful, does not qualify as "unlawful conduct" for the purposes of this tort. [At paras. 36-8; emphasis added.]

(See also *Rummery v. Matthews*, 2000 MBQB 67 (Man. Q.B.), var'd on other grounds, 2001 MBCA 32 (Man. C.A.); *Lerik v. Zaferis* (1929), [1930] 1 D.L.R. 634 (B.C. C.A.); and G.H.L. Fridman, *The Law of Torts*, *supra*, at 769-771.)

50 In my view, the misconduct of the Personal Defendants in this case — essentially the preparation of false records and reports sent by JingJing to XY and the breach of confidence found by the trial judge — satisfies in law the "unlawful act" requirement for these purposes.

Factual Findings

51 I turn next to the trial judge's findings concerning the conduct of Ms. Tang and Ms. Zhou, which counsel submit should not have attracted liability either in deceit or civil conspiracy. Ms. Tang was the lab manager in charge of embryo production and later semen production. She contends that she was a "mere employee" of JingJing and was following orders when she assisted Mr. Zhu in falsifying records in preparation for reporting sales to XY. She testified, for example, that "Jesse [Zhu] and Richard [Remillard]" are my direct supervisor[s]. I would do whatever they say." Similarly, Ms. Zhou, who was JingJing's bookkeeper, testified that as far as she was concerned, Mr. Zhu was "the boss". She recalled that when she had sent an e-mail to XY reporting numbers of embryo sales that she knew to be false, Mr. Zhu told her he was not sure whether "we will use them all or not". In response to Mr. Wilson's question as to whether he had told her the numbers were being falsified because JingJing "didn't want to pay the royalty on the embryos", she stated:

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> He told me that — he asked me not to worry because he said that he and Richard will address the issue later on, and also that he told me that, for the product that we exported to China, he's not sure — he's not sure whether he'll use all of the product or not. But that [is] what he told me.

52 The trial judge was not persuaded by this and similar evidence from either Ms. Zhou or Ms. Tang. In connection with the tort of deceit, he found that all three Personal Defendants "knew the information they provided to XY was false and [that] the circumstances warrant an inference that they intended for XY to be deceived by it." (Para. 247.) In his analysis:

> The basis of this conclusion rests on the factual findings regarding the meeting the four managers allegedly held[,] the documentary evidence in responses to emails and witnesses' testimony in court. Little credence can be given to Zhu, Zhou and Jin's evidence. Dr. Remillard had no reason to be untruthful. It is fair to conclude that such a meeting was held and that the managers there devised the plan to deceive XY.
>
> Following on Perell's discussion [see Paul Perell, "The Fraud Elements of Deceit and Fraudulent Misrepresentation" (1996), 18 *Advocates' Q.* 23 at 28-30] of intention in civil fraud, the following circumstances indicate liability for JingJing, Jesse Zhu, Selen Zhou and Tang Jin:
>
> • The email sent by Remillard to Zhu on Feb 18, 2004, stating that they have to be careful in selling sexed semen in China for which they had no licensing permission and to be wary of XY's inferences from the fact that they have so many SX cytometers. Remillard's statement, "I bet they have good lawyers too!" underlines the deception;
>
> • The meeting held by Tang Jin, Selen Zhou, Richard Remillard, and Jesse Zhu is evidence of [an] intention to produce deceiving numbers that only appear authentic; they agreed that the "[t]otal number of embryos would equal the number of doses we use per day." As Remillard testifies, the purpose of this endeavour was "to pay less royalty fee". Based on this meeting, it can be inferred that the defendants intended to lie and deceive XY by making representations that were contrary to the facts (or made in the absence of any facts).
>
> On June 21, 2006, Selen Zhou attempted to "renegotiate" the royalty terms by unilaterally altering the CLA. Dr. Jacobson rebukes her in an email for this and makes it clear that this is not the way he does business. He further requests that Zhou respond to Thom Gilligan's email "which seeks the correct details of your past sales — for reporting, royalty and compliance purposes."
>
> From this interaction it is clear that Zhou knew what royalties JingJing was responsible for to XY — why else would she attempt to actually alter the CLA? Altering the agreement is contrary to the defendants' assertion of a mistake of fact or honest belief and is circumstantial evidence that Selen Zhou actively perpetuated the deceit on XY by forwarding information she knew was false and was related directly to the payment provisions of the CLA.
>
> On June 20, 2007, Thom Gilligan sent an email to Remillard stating that he was skeptical of JingJing's reported numbers and challenging the reduced royalty rate on "B" type embryos. XY here is again informing JingJing that it is not complying with the expectations of the CLA. Remillard then immediately informs the other three managers that "the number given to XY must match...". The email on its face shows Remillard reaching out to the group to try and find a solution to a problem that affects all of their deceitful intentions.
>
> Further, the fact that Tang Jin sent an email to Remillard, Zhou and Zhu two days later (June 22, 2007), laying out just how the numbers could be massaged to fit XY's expectations indicates her participation in the actual deception. The email belies any suggestion she was simply following orders and appears as a voluntary offering of information to perpetuate the deception.

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The evidence establishes that Zhou knew the royalty terms of the CLA and was dissatisfied with them. She then knowingly reported false numbers; Tang volunteered information to assist in perpetuating the deception. [At paras. 248-54; emphasis added.]

53 Later, in connection with the tort of civil conspiracy specifically, he observed:

On the evidence before me, I am satisfied that there [was] an agreement. Dr. Remillard testified that in a meeting involving Tang Jin, Selen Zhou, Jesse Zhu and himself, they agreed what to report to XY with the purpose being to pay them the royalties to which XY was entitled [*sic*; "less than" the royalties to which XY was entitled?]:

Q During your discussion with Jesse Zhu and Tang Jin and Selen Zhou about the numbers you were going to produce — to disclose to XY — to report to XY, why did you decide to report a different number of embryos to XY than what you were actually making?

A We had to pay less royalty fee.

Even in the absence of such a meeting, there was, on all the evidence, clearly an agreement among the four principals. [At paras. 269-70.]

54 The trial judge also considered whether it was necessary for the plaintiff to prove that *each* conspirator must have committed an unlawful act for the tort to be made out, as suggested in *Bank of Montreal v. Tortora*, *supra*; but the Court here reasoned that:

. . . Chaisson [J.A.'s] final statement [in *Tortora*] cannot be applied in the manner suggested by the defendants. That case pertained to the striking of pleadings where the plaintiff did not plead specific unlawful acts carried out by one of the defendants, who allegedly participated in the conspiracy.

It was put this way in *Golden Capital Securities* at para. 74:

A person who conspires with others to commit unlawful acts may be liable for the consequences even though some of the acts are instigated by a single conspirator. But a person's liability for the acts of other conspirators requires proof that the person knew or should have known that such acts were a probable consequence of carrying out the common objective: *R. v. Henderson*, [1948] S.C.R. 226 at 236, [1949] 2 D.L.R. 121, as cited in *Claiborne* at 79. [At paras. 273-74.]

Applying *Golden Capital Securities*, the judge concluded:

I have found the defendants Jesse Zhu, Tang Jin and Selen Zhou liable for deceit. Additionally, in committing those unlawful acts, I am satisfied that these defendants knew or ought to have known that injury to the plaintiff was likely. These defendants were falsely reporting production and thereby underpaying the plaintiff.

Finally, I find that the plaintiff <u>suffered a financial loss as a result of the unlawful conduct by the defendants. It was deprived of the royalties to which it was entitled</u>.

For these reasons I concluded that the plaintiff has proved conspiracy on the part of Jesse Zhu, Selen Zhou and Tang Jin. [At paras. 275-77; emphasis added.]

55 Mr. Wilson referred us to various other references in the Court's reasons to evidence that fully supports the conclusions that the Personal Defendants were part of the "management team" of JingJing who not only acted in concert to carry out unlawful acts that would injure the plaintiff, but who assisted in planning how best to go about it. In my view, the evidence makes it impossible to say the judge erred in reaching these conclusions.

Employment Status

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56 The next issue is whether the trial judge erred in law in finding that the Personal Defendants, who were presumably acting in the course of their employment, could be personally liable for the tort of civil conspiracy (or deceit, assuming the element of reliance was proven). Put another way, does the fact that they were employees of JingJing shield them from the consequences of what would otherwise be tortious conduct?

Case Law

57 Surprisingly, the case law concerning the liability of employees who on the orders of or at the request of their employer commit torts or other wrongful acts that injure a third party, is not fully developed. One of the complicating factors is that many of the cases have arisen only in the context of applications to strike out pleadings and have not been decided on the merits. Another complication is due to the fact that the employers in most of the cases are corporations. A corporation can of course act only through its agents and employees and thus it can be said in a sense that any employee who commits a tort in the course of his or her duties is acting as his or her employer's agent. For economic reasons, the injured third party usually looks to the corporation rather than the employee for recovery.

58 The seminal English case is *Said v. Butt*, [1920] 3 K.B. 497 (Eng. K.B.), where McCardie J. reasoned as follows in connection with an action against a "servant" for inducing breach of contract on the part of his "master":

> ... the servant who causes a breach of his master's contract with a third person seems to stand in a wholly different position. He is not a stranger. He is the alter ego of his master. His acts are in law the acts of his employer. In such a case it is the master himself, by his agent, breaking the contract he has made, and in my view an action against the agent under *the Lumley v. Gye* [[1853] EWHC QB J73] principle must therefore fail, just as it would fail if brought against the master himself for wrongfully procuring a breach of his own contract ...
>
> I hold that if a servant acting *bona fide* within the scope of his authority procures or causes the breach of a contract between his employer and a third person, he does not thereby become liable to an action of tort at the suit of the person whose contract has thereby been broken. [At 505-6; emphasis added.]

However, McCardie J. added:

> Nothing that I have said today is, I hope, inconsistent with the rule that a director or a servant who actually takes part in or actually authorizes such torts as assault, trespass to property, nuisance, or the like may be liable in damages as a joint participant in one of such recognized heads of tortious wrong. [At 506; emphasis added.]

59 The scope of these remarks has given rise to much discussion and debate in the cases. I do not propose to trace that debate here; but counsel referred us to some recent Canadian authorities that illustrate how courts have treated the socalled '*Said v. Butt* exception' to the "general rule that persons are responsible for their own conduct." (See *ADGA Systems International Ltd. v. Valcom Ltd.* (1999), 168 D.L.R. (4th) 351 (Ont. C.A.) at para. 15.)

60 A 1995 case illustrates courts' reluctance to extend liability to employees of corporations for their employers' wrongs, although cases of fraud or dishonesty seem always to have constituted an exception to that approach. In *Montreal Trust Co. of Canada v. ScotiaMcLeod Inc.* (1995), 129 D.L.R. (4th) 711 (Ont. C.A.), the motions judge had struck out pleadings in an action brought against the directors of a company ("Peoples") that had issued debentures by means of a prospectus. The plaintiffs, who had purchased the debentures, claimed they had relied on certain misrepresentations in the prospectus. Importantly, they did not allege that they had placed any reliance on the actions of the directors "as a board or as individual directors", and the pleadings were silent on "significant particulars concerning the actions of the respondents as directors *simpliciter*." (At 717.) The plaintiffs took the position, however, that all the directors were "collectively responsible as joint tortfeasors" with Peoples. Thus in the words of Finlayson J.A. for the Court of Appeal, the cause of action pleaded was "predicated on personal liability *arising out of the actions of Peoples*." (At 720; my emphasis.) He continued:

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> The decided cases in which employees and officers of companies have been found personally liable for actions ostensibly carried out under a corporate name are fact-specific. In the absence of findings of fraud, deceit, dishonesty or want of authority on the part of employees or officers, they are also rare. Those cases in which the corporate veil has been pierced usually involve transactions where the use of the corporate structure was a sham from the outset or was an afterthought to a deal which had gone sour. ... In every case, however, the facts giving rise to personal liability were specifically pleaded. Absent allegations which fit within the categories described above, officers or employees of limited companies are protected from personal liability unless it can be shown that their actions are themselves tortious or exhibit a separate identity or interest from that of the company so as to make the act or conduct complained of their own.
>
> None of the conduct alleged against the respondent directors falls within the broad categories I have outlined above. Their exposure, if there is any, is narrowly focussed on their formal decision-making in the name of Peoples. A corporation may be liable for contracts that its directors or officers have caused it to sign, or for representations those officers or directors have made in its name, but this is because a corporation can only operate through human agency, that is, through its so- called "directing mind". Considering that a corporation is an inanimate piece of legal machinery incapable of thought or action, the court can only determine its legal liability by assessing the conduct of those who caused the company to act in the way that it did. This does not mean, however, that if the actions of the directing minds are found wanting, that personal liability will flow through the corporation to those who caused it to act as it did. To hold the directors of Peoples personally liable, there must be some activity on their part that takes them out of the role of directing minds of the corporation. In this case, there are no such allegations. [At 720-1; emphasis added.]

61 In the result, the Court struck out the action as against certain officers of Peoples, but allowed it to proceed as against two directors and senior executives who had been "involved in making certain representations personally which were relied upon by the appellants". (At 724-5.) I emphasize the Court's reference to cases of "fraud, deceit [or] dishonesty" as an exception to the general rule enunciated at the end of the passage.

62 In 1999, in *ADGA Systems*, the Ontario Court of Appeal was again asked to consider the "troublesome issue" of when corporate directors and employees may be liable for acts done "in pursuance of a corporate purpose". The plaintiff "ADGA" complained that a competitor, the defendant "Valcom", had "raided" the plaintiff's employees and used their names in a tender document in direct competition with ADGA's tender offer. The defendant was the successful bidder. ADGA sued Valcom for interference with economic interests, and sued a director and two employees of Valcom for their part in that tort and for inducing breaches of fiduciary duty on the part of its (the plaintiff's) employees. The lower court relied on *ScotiaMcLeod Inc.* (cited as *Montreal Trust Co. of Canada v. ScotiaMcLeod Inc.* (1995), 129 D.L.R. (4th) 711 (Ont. C.A.)) to rule that since Valcom's director and employees had not been furthering their own interests but were acting to further their employer's interests, no cause of action was sustainable against them.

63 On appeal, Carthy J.A. for the Court rejected the proposition that employees of corporations are always protected from liability for wrongs committed, or also committed, by their employers. He formulated the question as "whether, on the assumption that the defendant Valcom committed a tort against the appellant, the sole director and employees of Valcom can be accountable *for the same tort* as a consequence of their personal involvement directed to the perceived best interests of the corporation." (Para. 8; my emphasis.) He continued:

> My first observation is that I recognize the policy concern expressed by the Divisional Court, and other General Division judges, over the proliferation of claims against officers and directors of corporations in circumstances which give the appearance of the desire for discovery or leverage in the litigation process. This is a proper concern because business cannot function efficiently if corporate officers and directors are inhibited in carrying on a corporate business because of a fear of being inappropriately swept into lawsuits, or, worse, are driven away from involvement in any respect in corporate business by the potential exposure to ill-founded litigation. That being said, it is not appropriate to extend the reasoning of *ScotiaMcLeod* beyond its intended application by reading it

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> as protecting all conduct by officers and employees in pursuit of corporate purposes. The common law should not develop on an *ad hoc* basis to put out fires. When a policy issue arises, here from modern business realities, the courts must proceed on a principled basis to establish a framework for further development which recognizes the new realities but preserves the fundamental purpose served by that area of law ... [At para. 9; emphasis added.]

64 With respect to *Salomon v. Salomon & Co.* (1896), [1895-99] All E.R. Rep. 33 (U.K. H.L.), the Court observed that where a plaintiff seeks to establish an "independent" cause of action against the principals of a company, *Salomon* is not engaged and the corporate veil is not threatened. The distinction between an "independent" cause of action and "looking through the corporation" had been confirmed, Carthy J.A. stated, by *Said v. Butt*. In his analysis:

> First, this [*Said v. Butt*] is not an application of *Salomon v. Salomon*. That case is not mentioned anywhere in the reasons. Second, it provides an exception to the general rule that persons are responsible for their own conduct. That exception has since gained acceptance because it assures that persons who deal with a limited company and accept the imposition of limited liability will not have available to them both a claim for breach of contract against a company and a claim for tortious conduct against the director with damages assessed on a different basis. The exception also assures that officers and directors, in the process of carrying on business, are capable of directing that a contract of employment be terminated or that a business contract not be performed on the assumed basis that the company's best interest is to pay the damages for failure to perform. By carving out the exception for these policy reasons, the court has emphasized and left intact the general liability of any individual for personal conduct. [At para. 15; emphasis added.]

65 Carthy J.A. added at para. 18 that:

> The consistent line of authority in Canada holds simply that, in all events, officers, directors and employees of corporations are responsible for their tortious conduct even though that conduct was directed in a *bona fide* manner to the best interests of the company, always subject to the *Said v. Butt* exception.
>
> [Emphasis added.]

As examples, he referred to *Lewis v. Boutilier* (1919), 52 D.L.R. 383 (S.C.C.), at 389; *Berger v. Willowdale A.M.C.* (1983), 41 O.R. (2d) 89 (Ont. C.A.), at 98, *lve to app ref'd* May 17, 1983 [(1983), 41 O.R. (2d) 89n (S.C.C.)]; *Desrosiers v. Sullivan* (1986), 76 N.B.R. (2d) 271 (N.B. C.A.), *lve to app ref'd* June 4, 1987 [(1987), 40 C.C.L.T. 66n (S.C.C.)]. In the latter case, Hoyt J.A. had reasoned:

> The question here, as I have pointed out, is not whether Mr. Sullivan was acting on behalf of or even if he "was" the company, but whether a legal barrier, here a company, can be erected between a person found to be a wrongdoer and an injured party thereby relieving the wrongdoer of his liability. In my opinion, once it is determined that a person breaches a duty owed to neighbouring landowners not to interfere with their reasonable enjoyment of their property, liability may be imposed on him and he may not escape by saying that as well as being a wrongdoer he is also a company manager or employee. [At 278; emphasis added.]

And in an earlier case of alleged fraud, *Kepic v. Tecumseh Road Builders* (1987), 18 C.C.E.L. 218 (Ont. C.A.), Brooke J.A. had stated for the Court:

> It is well established that the directors of a corporation will not be liable for inducing that corporation to breach its contract when they are performing *bona fide* their functions as corporate officers. See *Said v. Butt*... This is not the case where a director acts in a fraudulent manner: Fraudulent efforts by a director of a corporation to increase the revenue of that body cannot be said to be *bona fide* in its best interest. See generally *Einhorn v. Westmount Investments Ltd.* (1969), 69 W.W.R. 31, 6 D.L.R. (3d) 71 (Sask. Q.B.), affirmed (1970), 73 W.W.R. 161, 11 D.L.R. (3d) 509 (Sask. C.A.); *McFadden v. 481782 Ontario Ltd.* (1984), 47 O.R. (3d) 134, 5 C.C.E.L. 83, 27 B.L.R. 173, (Ont. H.C.). [At 222; emphasis added.]

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This passage was approved by the Court in *ADGA*.

66 Carthy J.A. also considered the seminal Canadian case on vicarious liability, *London Drugs Ltd. v. Kuehne & Nagel International Ltd.*, [1992] 3 S.C.R. 299 (S.C.C.). The majority there rejected the argument that generally in Canada "an employee acting in the course of his or her employment and performing the 'very essence' of his or her employer's contractual obligations with a customer does not owe a duty of care, whether one labels it 'independent' or otherwise, to the employer's customer." (At 407-8.) (LaForest J. in dissent also spoke in terms of "the employee's primary duty" owed to third parties who might be injured in the course of the employee's duties: see 339.) The *ADGA* Court stated in summary that:

> These Canadian authorities at the appellate level confirm clearly that employees, officers and directors will be held personally liable for tortious conduct causing physical injury, property damage, or a nuisance even when their actions are pursuant to their duties to the corporation." [At para. 26.]

67 After referring to *Normart Management Ltd. v. West Hill Redevelopment Co.* (1998), 37 O.R. (3d) 97 (Ont. C.A.); *Alper Development Inc. v. Harrowston Corp.* (1998), 38 O.R. (3d) 785 (Ont. C.A.) and other authorities, Carthy J.A. concluded in *ADGA that* there was no principled basis for protecting the director and employees of Valcom from liability for their alleged conduct and that the law in this area should be permitted to develop over time in a principled way. The action against the individual defendants was allowed to proceed.

68 Both *ScotiaMcLeod* and *ADGA* were discussed by this court in *Hildebrand v. Fox*, 2008 BCCA 434 (B.C. C.A.), which again concerned an application to strike pleadings under R. 19(24) of the then *Rules of Court*. The plaintiff in that case, a teacher employed by the defendant school board, alleged gross negligence on the part of the superintendent of the board, Mr. Fox, in failing to meet the standard of care owed to her in investigating a complaint against her and reporting to the board. In support of his objection that no independent cause of action lay against him, the defendant relied on various cases, including *ScotiaMcLeod*, for the proposition that employees will not be liable for acts done in the course of their employment "unless the employee commits a tortious act which demonstrates an identity or interest separate and apart from their employer." (Para. 46.) For her part, the plaintiff relied on *London Drugs* as demonstrating that an employee can be liable in negligence "alongside his or her employer".

69 Tysoe J.A. in *Hildebrand* reviewed *Said v. Butt* and many of the cases mentioned above, ending with *London Drugs*. He observed that there is "no clear consensus" as to the law concerning the personal liability of employees, but continued:

> The law is relatively clear that, based on *Said v. Butt*, an employee of a company which has breached a contract is not personally liable for the tort of inducing breach of contract or for another claim that is a disguised attempt to make a non-party liable on a contract. That is not the situation in this case. Based on *London Drugs* and *ADGA Systems*, it is at least arguable that the principle in *Said v. Butt* does not extend to the tort of negligence even where the negligent act or omission occurred in the performance by the employee of a contract between the employee's corporate employer and the plaintiff. [At para. 70; emphasis added.]

The Court held that it was not plain and obvious the pleadings failed to disclose a cause of action against Mr. Fox "on the ground that it fails to demonstrate that he had an identity or interest separate and apart from [that of] the Board." (Para. 71.)

70 Finally in this line of authorities, we were referred to *Strata Plan No. VIS3578 v. Canan Investment Group Ltd.*, 2010 BCCA 329 (B.C. C.A.). The Court in that instance addressed several questions, including whether the chambers judge below had erred in dismissing an application to join certain persons as defendants in a larger action involving a "leaky condo". Neilson J.A. referred *inter alia* to *London Drugs, Said v. Butt, ScotiaMcLeod, Hildebrand*, and a decision of the British Columbia Supreme Court, *Strata Plan LMS 2262 v. Stoneman Developments Ltd.*, 2004 BCSC 828, 39 C.L.R. (3d) 127 (B.C. S.C.). In *Stoneman*, Garson J. (as she then was) had suggested that a "dichotomy" existed in British Columbia between authorities which hold that "an employee is not personally liable unless his actions are themselves tortious *and*

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exhibit a separate identity or interest from that of the company", and others to the effect that "an independent tort is not required, and that an employee or director may be sued personally if his actions are tortious *or* exhibit a separate identity or interest from that of the company." (Para. 87; my emphasis.)

71 Neilson J.A. in *Neilson* disagreed that such a dichotomy existed (see para. 69) and found it was not plain and obvious that claims in negligence against the individual respondents personally would be excluded under the "*Said v. Butt* exception to the general principle outlined in *London Drugs*". In her analysis:

> The fact that a director, officer or employee was acting within the course of employment and the corporation is vicariously liable for his negligence does not preclude a claim in negligence against the employee personally. However, in my view, the *London Drugs* principle requires that the claim against the individual must be based on the breach of a duty of care that would support an action against the individual personally. The material facts that support that personal claim in tort must be specifically pleaded to establish a possible cause of action under R. 15(5)(a)(iii). [At para. 66; emphasis added.]

72 It does not appear that the foregoing authorities were cited to the trial judge in the case at bar. He referred only to a passage from Peter T. Burns and Joost Blom, *Economic Interests in Canadian Tort Law* (2009), where the authors stated:

> A fraudulent employee or agent is, of course, liable jointly with the employer or principal, irrespective of whether the fraud was done at the behest and for the benefit of the latter. [At 76.]

Curiously, the two cases cited by the authors (and mentioned by the trial judge at para. 256 of his reasons) are of little assistance on the question of employees' liability, given that they did not differentiate between defendant employees and defendant employers.

73 Nevertheless, it appears to be the law in Canada that as long as tortious conduct on the part of an employee or agent of a corporation (or any other employer) is properly pleaded and proven as an "independent" tort by the employee or agent, the wrongdoer can be held personally liable notwithstanding that he or she may have been acting in the best interests of (and at the behest of) the employer or principal. I see no reason in principle or policy why such liability should be restricted to cases involving physical damage (as *Said v. Butt* may have suggested in 1920), or to claims in negligence (as referred to in *London Drugs*, *Hildebrand* and *Neilson*.) Certainly the Ontario Court of Appeal did not so restrict it in *ADGA*. (See also *Hogarth v. Rocky Mountain Slate Inc.*, 2013 ABCA 57 (Alta. C.A.) at para. 103; *Schembri v. Way*, 2012 ONCA 620 (Ont. C.A.) at para. 30; *Correia v. Canac Kitchens*, 2008 ONCA 506 (Ont. C.A.) at paras. 86-8; and *Unisys Canada Inc. v. York Three Associates Inc.* (2001), 150 O.A.C. 49 (Ont. C.A.) at para. 11.)

74 In any event it is clear that fraud or fraudulent conduct has historically fallen into an established category in which personal liability has been imposed on agents and employees. It is sufficient in the case at bar to rely on this exception, although the acts of the Personal Defendants were properly pleaded as amounting to civil conspiracy and in this sense constituted a tort that was independent of that alleged against JingJing.

75 In the result, it cannot in my view be said that the claims of deceit or civil conspiracy were not available to XY against the Personal Defendants as a matter of law merely because they were employees of JingJing and acting in the course of their duties to further the objectives of JingJing.

"Following Orders" Defence?

76 Counsel for Ms. Zhou and Ms. Tang did not frame their challenge to personal liability in terms of the *Said v. Butt* line of cases, however. Instead they argued that in carrying out the conduct complained of, they were "only following orders" and could not be expected to refuse to carry out the scheme apparently devised by their boss, Mr. Zhu. (As earlier mentioned, he was the directing mind of JingJing and the IND Group.) Counsel referred us to evidence that both Ms. Zhou and Ms. Tang were receiving modest salaries from JingJing — although Mr. Wilson also referred us to evidence that they worked for other IND companies and may have been remunerated more substantially in other ways.

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77 It is a striking fact that no case was cited to us in which the "following orders" argument was advanced, much less successfully, in a context analogous to this case. Mr. Gudmundseth referred us to a decision of the Federal Court of Australia in *Cooper v. Universal Music Australia Pty. Ltd.*, [2006] FCAFC 187 (Australia Fed. Ct.), a copyright infringement case involving a website that contained hyperlinks to remote websites which users could use to have music transmitted directly to their computers. The website was hosted by "ComCen" and was owned and operated by the defendant Mr. Cooper. He was found to have "authorized" the infringement of copyright in sound recordings within the meaning of s. 101(1A) of the *Copyright Act 1968*, as was the defendant Mr. Takoushis, who supplied computing "support services".

78 In the course of its lengthy reasons on appeal, the Court addressed the question of whether Mr. Takoushis had in law "authorized" the infringement:

> Mr Takoushis had studied information technology at TAFE before becoming an employee of Com-Cen. He gave evidence that his position within that company was essentially a computing support role. His Honour found that Mr Takoushis was Mr Cooper's primary contact with Comcen and that he provided assistance from time to time in relation to the establishment and operation of Mr Cooper's website.
>
> The evidence did not establish that Mr Takoushis had any personal power to prevent the doing of the acts of copyright infringement (s 101(1A)(a)). He was not Mr Cooper's internet service provider; he was merely an employee of the internet service provider — albeit an employee with skills in computer technology who undertook work in relation to Mr Cooper's website.
>
> Nor did the evidence establish that there was any relevant relationship between Mr Takoushis and the users of Mr Cooper's website or between Mr Takoushis and the operators of the remote websites from which sound recordings were communicated (s 101(1A)(b)). Nor did the evidence suggest that there was any reasonable step open to be taken by Mr Takoushis personally to prevent or avoid the doing of the acts of copyright infringement. While it would have been a reasonable step for Mr Takoushis' employer to have terminated its hosting of Mr Cooper's website, either absolutely or unless he removed the hyperlinks on it which facilitated copyright infringement, the evidence did not establish that Mr Takoushis had the necessary authority to do so himself (s 101(1A)(c)). I do not consider that it would have been a reasonable step for Mr Takoushis to approach his employer to compel them to do so.
>
> ... Mr Takoushis was not a director of either Com-Cen or E-Talk. Nor was he shown to be an executive or shareholder of either of those companies. His evidence that his position within Com-Cen was essentially a computing support role was not challenged.
>
> In my view, the evidence before the primary judge was insufficient to establish that Mr Takoushis infringed the Record Companies' copyright by personally authorizing the relevant acts of copyright infringement.
>
> Further, for the reasons given above, the evidence before the primary judge was insufficient to demonstrate that Mr Takoushis held an executive or managerial role within either Com-Cen or E-Talk such that his involvement with their acts of copyright infringement rendered him personally liable for those acts of copyright infringement ... [At paras. 69-74; emphasis added.]

The Personal Defendants Zhou and Tang rely on this reasoning for the proposition that a person who holds a merely supportive role should not be held liable for participation in wrongs devised by and carried out by her employer.

79 There is no doubt that the implications of holding an employee responsible for 'supporting' or 'assisting' her employer in what turns out to be fraudulent conduct, must be carefully considered. As Southin J. (as she then was) stated in *United Services Funds (Trustee of) v. Lazzell* (1988), 28 B.C.L.R. (2d) 26 (B.C. S.C.):

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> One must, I think, be wary of postulating so wide a theory of assistance as to make liable, for instance, a secretary or bookkeeper who, discovering that her employer is engaged in chicanery, simply goes on doing the duties, not tortious in themselves, he or she did before. [At 89.]

I agree that the employee who simply carries on doing the job she has always done, notwithstanding that her typing or bookkeeping may assist in a fraud, should not without more be regarded as a fraudster (or conspirator) herself. (As noted by the Law Reform Commission of British Columbia in its *Report on Shared Liability* (1986) at 25-6, a person in this situation who "acts innocently or is unaware of the tortious act of another" would be entitled to indemnification from the employer.)

80 Here, however, the trial judge found that Ms. Zhou and Ms. Tang went beyond mere bookkeeping or 'typing' lab reports at Mr. Zhu's instructions. Both defendants *actively* assisted in devising how best to deceive XY. Their acts were, then, "tortious in themselves" and were not part of their regular duties. As stated by Burns and Blom, *supra*, it appears the law has historically held fraudulent employees liable with their employers "irrespective of whether the fraud was done at the behest and for the benefit of the latter." As for *Cooper v. Universal Music Australia Pty. Ltd.*, I regard the reasoning relied on by the defendants as confined to the meaning of "authorized" in the Australian *Copyright Act 1968*.

81 In the result, I would reject the "following orders" defence asserted on behalf of Ms. Tang and Ms. Zhou.

The IND Corporate Defendants

82 At para. 297 of his reasons, the trial judge turned to the question of whether the Personal Defendants were "together with the corporate IND defendants, jointly and severally liable" for the tort of deceit. (Obviously, this question does not arise unless JingJing was indeed liable in deceit.) The Court referred to *Osborne v. Pavlick*, 2000 BCCA 120 (B.C. C.A.), where Southin J.A. adopted Scrutton L.J.'s description of "joint tortfeasors" in *"Koursk" (The), Re*, *supra*:

> The substantial question in the present case is: What is meant by "joint tortfeasors"? and one way of answering it is: "Is the cause of action against them the same?" Certain classes of persons seem clearly to be "joint tortfeasors": The agent who commits a tort within the scope of his employment for his principal, and the principal; the servant who commits a tort in the course of his employment, and his master; two persons who agree on common action, in the course of, and to further which, one of them commits a tort. These seem clearly joint tortfeasors; there is one tort committed by one of them on behalf of, or in concert with another. [At 155; emphasis added.]

The trial judge found that on the evidence, XY had not established that "the tort of deceit committed by the [Personal Defendants] was in concert with the corporate members of the IND Group (beyond JingJing), or that it was committed on their behalf." (Para. 298.)

83 XY submits on its appeal that there is no basis in the evidence to differentiate the Personal Defendants' relationship with JingJing from their relationship with any other company in the IND Group. The plaintiff's factum elaborates:

> ... Ms. Tang and Ms. Zhou both worked for the IND Group generally. That is the way their contracts were written; that is the way they worked; that is the way they were remunerated; and that is the way they thought of it themselves. As agents or employees of all of the members of the IND Group, their joint conduct with Mr. Zhu attracts liability for the IND Group as a whole. The trial judge's findings in respect of JingJing inexorably lead, on this record, to the same conclusion in respect of the remainder of the corporate group.
>
> The record well illustrates the way in which the conduct of the individual defendants engaged and involved the various companies in the IND Group. Under Ms. Tang's direction, IND Embryontech produced sexed IVF embryos in Quebec (TJ, paras. 23, 308), and IND (Pennsylvania) and IND (California) produced such embryos in their respective jurisdictions (TJ, paras. 24, 25, 308). In that same capacity, and working from those same labs, Ms. Tang generated the false data that Ms. Zhou eventually supplied to XY, with Mr. Zhu's approval (TJ, para. 89.)

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> To the same effect, when JingJing purported to make an honest and comprehensive reporting in 2008, it did so using a false "embryo implant table", prepared by Ms. Tang using data generated by IND (Qingdao), describing the IND Group's embryo usage in China ... That table was then relied on by Ms. Tang at trial ...
>
> JingJing itself never even possessed the documents or the data that [were] used to deceive XY in respect of IVF embryo production. That was established when, in the course of document production, JingJing was revealed not to have any such materials in its possession or control. The magnitude of the IND Group's common fraud was only revealed to XY when it obtained production from what were then called the "non-licensee defendants"-i.e., the IND Group companies other than JingJing ...
>
> [Emphasis added.]

In summary, counsel submits that the Personal Defendants were not acting on behalf of JingJing alone when they perpetrated their fraud, but that Ms. Tang in particular:

> ... used her employment relationships (*qua* lab manager) with all of those companies to falsify their records and contrive the numbers that were at the core of the false reporting that, in the language of Scrutton L.J. [in *The Koursk*] was the subject of her "common action" with JingJing and the other individuals ... In this way, the [Personal Defendants] were the human nexus that bound the IND Group together, and enabled the companies' common fraud.
>
> [Emphasis added.]

84 The argument, then, is that because Ms. Tang and Ms. Zhou worked for some, if not all, of the corporate defendants, they must be taken to have falsified the reports required to be made to XY under the CLA, in their capacity as employees of those other corporations. The fact remains, however, that it was in the course of their duties as employees of *JingJing* that Ms. Tang and Ms. Zhou conspired to injure XY by means of the falsified documents. Only JingJing was a party to the CLA, and only JingJing was required to report its revenues from the use of the technology. The fact Ms. Tang and Ms. Zhou may have used some IND facilities does not amount to proof that they were acting on behalf of or for the benefit of the other corporations. In my view, the trial judge correctly rejected this theory of 'infective liability' advanced by XY.

85 In the alternative, XY submits that the trial judge should have "collapsed" the separate legal personalities of the IND corporations into one (presumably JingJing) and should have treated its conduct as that of the IND Group as a whole. It is said the trial judge erred in applying "the wrong test" in rejecting this "group enterprise" submission.

86 The law concerning both the lifting of a corporate veil in a simple 'Salomon' situation, and disregarding the separate personality of a group of related corporations is highly fact-dependent and does not admit of any clear test or rules. As Professor McGuinness observes in *Canadian Business Corporations Law* (2nd ed., 2005), it is difficult to make out any general principle followed by the courts in handling such cases. (At 49.) The trial judge referred to *Smith, Stone & Knight Ltd. v. Birmingham (City)*, [1939] 4 All E.R. 116 (Eng. K.B.), a case about the lifting of the corporate veil of a subsidiary to implicate its parent company. Atkinson J. there acknowledged that notwithstanding the separate legal personality of a corporation, there "may be such an arrangement between the shareholders and a company as will constitute the company the shareholders' agent for the purpose of carrying on the business and make the business the business of the shareholders." He continued:

> It seems therefore to be a question of fact in each case, and those cases indicate that the question is whether the subsidiary was carrying on the business as the company's business or as its own. I have looked at a number of cases — they are all revenue cases — to see what the courts regarded as of importance for determining that question ... and I find six points which were deemed relevant for the determination of the question: Who was really carrying on the business? ... The first point was: were the profits treated as the profits of the company? ... [S]econdly, were the persons conducting the business appointed by the parent company? Thirdly, was the company the head and the brain of the trading venture? Fourthly, did the company govern the adventure, decide what should be done

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and what capital should be embarked on the venture? Fifthly, did the company make the profits by its skill and direction? Sixthly, was the company in effectual and constant control? ... and it seems to me that every one of those questions must be answered in favour of the claimants. [At 121.]

87 I do not read the trial judge in the case at bar as having applied these (or any other) "tests". To the contrary, he said he was unable to answer them with any certainty: para. 314. He also noted the discussion of *Smith, Stone* in *Alberta Gas Ethylene Co. v. R.* (1988), 24 F.T.R. 309 (Fed. T.D.), at 313-14, where the Court took a "restrained" view of Atkinson J.'s comments. See also *Bow Valley Husky (Bermuda) Ltd. v. Saint John Shipbuilding Ltd.* (1995), 126 D.L.R. (4th) 1 (Nfld. C.A.) at paras. 38-51, *var'd*, [1997] 3 S.C.R. 1210 (S.C.C.); *Edgington v. Mulek Estate*, 2008 BCCA 505 (B.C. C.A.), at paras. 19-26; and most recently, the decision of the U.K. Supreme Court in *Prest v. Petrodel Resources Ltd.*, [2013] UKSC 34 (U.K. S.C.) at paras. 17-35 (*per* Lord Sumption JSC) and paras. 60-83 (*per* Lord Neuberger of Abbotsbury PSC). At para. 106 of *Prest* Lord Walker of Gestingthrope aptly summarized the state of the law:

> I am reluctant to add to the discussion but for my part I consider that "piercing the corporate veil" is not a doctrine at all, in the sense of a coherent principle or rule of law. It is simply a label — often, as Lord Sumption JSC observes, used indiscriminately — to describe the disparate occasions on which some rule of law produces apparent exceptions to the principle of the separate juristic personality of a body corporate reaffirmed by the House of Lords in *Salomon v. A Salomon & Co Ltd.* ... These may result from a statutory provision, or from joint liability in tort, or from the law of unjust enrichment, or from principles of equity and the law of trusts (but without any "false invocation of equity" in the phrase used by C Mitchell in the article mentioned by Lord Neuberger PSC, at para 77). They may result simply from the potency of an injunction or other court order in binding third parties who are aware of its terms. If there is a small residual category in which the metaphor operates independently no clear example has yet been identified. ...
>
> [Emphasis added.]

88 The leading decision of this court is *B.G. Preeco I (Pacific Coast) Ltd. v. Bon Street Holdings Ltd.* (1989), 60 D.L.R. (4th) 30 (B.C. C.A.). There, Seaton J.A. rejected the conclusion that courts should lift the corporate veil wherever "fair play and good conscience" indicate — the so-called "Deep Rock doctrine". He observed that the corporate veil has been pierced in instances of "fraud or improper conduct" where the corporation "is used to effect a purpose or commit an act which the shareholder could not effect or commit", citing *Gilford Motor Co. v. Horne*, [1933] Ch. 935 (Eng. Ch. Div.). The veil had also been pierced in tax cases involving corporate groups "so as to ignore the separate legal existence of related companies", and the group enterprise theory had on occasion been extended to non-tax cases. However, Seaton J.A. observed, the House of Lords had limited those cases to their facts in *Woolfson v. Strathclyde Regional Council*, [1978] Sess. Cas. (H.L.) 90 (Scotland H.L.) and in *Industrial Equity Ltd. v. Blackburn* (1977), 137 C.L.R. 567 (Australia H.C.), the Australian High Court had disapproved of the idea of "treating related companies as one entity, absent some specific statutory requirement".

89 Overall, the Court in *B.G. Preeco* was decidedly unenthusiastic about the idea of disregarding corporate personality. On the facts of *B.G. Preeco*, Seaton J.A. observed:

> ... the plaintiff knew it was dealing with a company. The fraud found by the trial judge caused the plaintiff to believe that the company had assets that it, in fact, did not have. That has nothing to do with the corporate veil. The use of a company as a means of avoiding bearing business losses is neither unusual nor a basis for lifting the veil.
>
> In my view, the proper remedy is not to lift the corporate veil, but to award damages for fraud against the individuals and the company that committed the fraud. That is what the trial judge did. [At 40; emphasis added.]

90 Counsel also referred us to the more recent case of *Transamerica Life Insurance Co. of Canada v. Canada Life Assurance Co.* (1996), 28 O.R. (3d) 423 (Ont. Gen. Div.). There Sharpe J. (as he then was) stated:

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> As just indicated, the courts will disregard the separate legal personality of a corporate entity where it is completely dominated and controlled and being used as a shield for fraudulent or improper conduct. The first element, "complete control", requires more than ownership. It must be shown that there is complete domination and that the subsidiary company does not, in fact, function independently: *Aluminum Co. of Canada Ltd. v. Toronto (City)*, [1944] S.C.R. 267 at p. 271, [1944] 3 D.L.R. 609; *Bank of Montreal v. Canadian Westgrowth Ltd.* (1990), 72 Alta. R. (2d) 319 (Q.B.). ...
>
> The second element relates to the nature of the conduct: is there "conduct akin to fraud that would otherwise unjustly deprive claimants of their rights"? [At 433-4; emphasis added.]

91 Fraud has of course been proven in this case and XY contends that there is evidence of conduct that satisfies the first element referred to in *Transamerica*: all the IND corporations are owned and/or controlled by Mr. Zhu, and he himself stated in discovery that until IND Dairy Tech Ltd. became publicly listed, "all the shareholding was in China and in Canada was controlled by me. [*Sic.*] It's an absolute common interest entity." (Para. 299.)

92 As the defendants contend, however, XY was not deceived by JingJing's separate legal personality *per se*. Presumably, XY dealt with JingJing in full knowledge that it was part of a larger group. XY did not insist upon receiving guarantees or other security from other members of the group as security for JingJing's performance of its obligations under the CLA. As in *BG Checo*, JingJing's fraud had "nothing to do" with the corporate veil. Moreover, Mr. Zhu, the individual who controlled JingJing's shareholder, has of course been found personally liable for the same damages as JingJing itself. It is thus unclear to me how the application of the "group enterprise" theory would assist the plaintiff in practical terms. At the least, if all the assets of the other IND corporations were to become available to satisfy XY's judgment, existing creditors of those corporations would be affected and would have legitimate objections.

93 XY also relies on another category of case described by the Court in *BG Checo* — where the corporation is used to "effect a purpose or commit an act which the shareholder could not effect or commit." (At 38.) In XY's submission, JingJing was established for the very purpose of allowing the other members of the IND Group to obtain XY's technology without paying for it. The plaintiff points to an e-mail sent by Dr. Remillard to Mr. Zhu on April 30, 2003:

> If we setup a new company for that project, we will only pay royalty on the semen, because no embryos will be produced by that company.
>
> [Emphasis added.]

In addition, XY asserts that "notional sales" from JingJing to other members of the Group were 'papered' to bring about JingJing's insolvency, leaving those corporations with XY's technology:

> ... to avoid the consequences of breaching the CLA, Mr. Zhu and the IND Group moved the property with which the CLA was concerned (i.e., sexed semen and IVF sexed embryos) into the hands of other IND Group companies, through notional sales papered after the fact without money changing hands. The effects of this were twofold. First, these notional transactions hollowed out JingJing financially. Ms. Zhou caused the "sale" of embryos to IND (Qingdao) through JingJing. This caused JingJing to accumulate debts owing to IND Embryontech (on paper, the original vendor). When IND (Qingdao) then failed to pay JingJing for the embryos, Mr. Zhu had thereby managed to contrive an artificial insolvency; JingJing could not pay its debts to IND Embryontech as they become due, leading to its bankruptcy and eliminating XY's recourse against JingJing for breach of the CLA. ... Second, the IND Groups shadowy internal dealings produced the "paucity of evidence" of enrichment that the trial judge found defeated XY's unjust enrichment claim against [it].
>
> [Emphasis added.]

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(Other acts of deceit, or at least involvement in some aspects of JingJing's deceit, on the part of other members of the IND Group are mentioned by the trial judge in passing at paras. 94, 95, 130, 131, 199 and 282 of his reasons.)

94 The IND corporations submit in response that there is "no evidence" that the shareholder(s) of JingJing used the corporate vehicle to effect a purpose that it or they could not otherwise effect. Yet if the evidence supports the allegations quoted above concerning JingJing's insolvency, it might well be said the corporate vehicle had been used essentially to rob XY of its technology (not only of royalties) and to thwart its legal remedies.

95 In these circumstances, it is unfortunate that the trial judge did not make findings of fact in response to XY's allegations on this point. It will be recalled that he stated at para. 317 only that the circumstances of this case and of the members of the IND Group did not "rise to a level where the consequences" of the torts of JingJing and the Personal Defendants or those of JingJing's breach of contract "should flow throughout the IND Group to its individual members." This was followed closely by the conclusion at para. 321 under the heading "Unjust Enrichment" that although detriment on XY's part and the absence of juristic reason had been proven, the third element — i.e., the enrichment of the IND defendants — had not.

96 In my view, it was not by chance that the group enterprise doctrine and the claim in unjust enrichment were considered at the same point in the Court's analysis. Both would have been means by which the benefits (if any) of the fraud that were allegedly passed on to other members of the IND Group upon JingJing's bankruptcy could be pursued by the plaintiff. As suggested above, the "group enterprise" doctrine would be a highly uncertain and improbable route, and might yield nothing but expense and delay. The unjust enrichment claim, on the other hand, would have been a more direct means of addressing XY's complaints with respect to the use of JingJing to "front" a relationship with XY for the purpose of moving its technology to one or more of the other corporations, and with respect to the "hollowing out" of JingJing by means of paper debts to IND Embyrontech.

97 In my respectful view it was incumbent on the trial judge to consider the evidence cited in this regard, to make findings of fact, and then to reach and explain his conclusions based thereon. While I am not persuaded he erred in declining to take the extreme step of notionally "collapsing" the separate identity of the IND defendants into one, I am driven to the conclusion that he did err as a matter of law in failing to analyze the evidence related to the claim for unjust enrichment and that that matter should be remitted to the court below for retrial as against the IND defendants. I would allow XY's appeal to the extent of revising para. 9 of the trial court's order as set out at the end of these reasons.

Injunctive Relief

98 As mentioned earlier, the terms of the CLA required JingJing (then known as IND Lifetech, Inc.) to keep XY's technology confidential. The Agreement defined the term "Technology" as follows:

> "Technology" means any and all Proprietary Rights or confidential information, trade secrets, know-how, technical data, masks, code, programs, designs, processes, methods, operations, innovations, or inventions, whether or not patented, and any patents, patent applications, copy rights, or other intellectual property of any kind that Licensor, now or hereafter, owns, controls, licenses, or has an interest in.

and "Proprietary Rights" thus:

> "Proprietary Rights" with respect to the Technology means the collection of all Patent Rights, Trademark Rights, Trade Secret Rights, and Copyright Rights, or other rights which are or may be asserted as protectable under the laws of the United States or the laws of any foreign country.

99 Section 3.10 of the CLA contained the central covenant regarding confidentiality and the exceptions thereto:

> CONFIDENTIALITY: Each of the parties to this License Agreement shall maintain and hold confidential any and all information regarding the terms or condition of this License Agreement and any and all information regarding

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the Technology, the Proprietary Rights, or Improvements thereto of the other party during the Term of this License Agreement and thereafter, except to the extent that the information:

i. is or becomes generally available to the public other than as a result of a disclosure by the recipient party;

ii. becomes available to recipient party on a nonconfidential basis and not in contravention of applicable law from a source other than the other party or one of its officers, directors, partners, employees, independent contractors, agents, or licensees ("Representatives") not bound by a confidential relationship with disclosing party or by a confidentiality or other similar agreement;

iii. can be proven was known by recipient party on a nonconfidential basis and not in contravention of applicable law or confidentiality or other similar agreement prior to disclosure to recipient party by disclosing party;

iv. notwithstanding the foregoing, with respect to the Licensed Technical Information or any information marked or indicated by the disclosing party as confidential, recipient party shall maintain such information as confidential.

Licensee agrees to limit access to information to employees or independent contractors who by express writing agree to confidentiality obligations including terms set out by Exhibit H (Assignment Agreement Terms) and Exhibit 1 (Nondisclosure Agreement Terms).

100 The trial judge considered the granting of injunctive relief beginning at para. 323 of his reasons. He noted *Qureshi v. Gooch*, 2005 BCSC 1584 (B.C. S.C.), where the Court in turn cited the leading Canadian case, *Cadbury Schweppes Inc. v. FBI Foods Ltd.*, [1999] 1 S.C.R. 142 (S.C.C.) for the proposition that in determining whether such relief is appropriate, the court considers the nature of the rights sought to be protected and the surrounding circumstances, and attempts to "balance the equities" between the parties. The Supreme Court confirmed that an action for breach of confidence is *sui generis*, a characterization said to "recognize the flexibility that has been shown by courts in the past to uphold confidentiality and in crafting remedies for its protection". (Para. 28.) Binnie J. cited with approval the observations of Deane J. in *Moorgate Tobacco Co. v. Philip Morris Ltd.* (1984), 156 C.L.R. 414 (Australia H.C.), at 438:

> Like most heads of exclusive equitable jurisdiction, its rational basis does not lie in proprietary right. It lies in the notion of an obligation of conscience arising from the circumstances in or through which the information was communicated or obtained.

On the facts in *Cadbury Schweppes* itself, the Court concluded that the circumstances of the parties' dealings and the nature of the information ("nothing very special") militated against the granting of a permanent injunction, and that a monetary remedy was adequate.

101 The trial judge in the case at bar also referred to Robert J. Sharpe, *Injunctions and Specific Performance* (looseleaf, 2010) for the proposition that an injunction will ordinarily be granted in the intellectual property context where (1) the plaintiff has a legal right in the property; (2) there is a real threat to or an actual invasion of the legal right; and (3) there is no defence of laches, delay, acquiescence or estoppel. (At para. 4.690, quoted at para. 327 of the trial judge's reasons; see also R. E. Dimock, *Intellectual Property Disputes: Resolutions and Remedies* (looseleaf, 2004) at 15.2, cited by the judge at para. 330.)

102 The trial judge found that injunctive relief was appropriate because XY had not sought damages for the future effects of JingJing's breach of confidence. In his analysis:

> If it were denied, the defendants would be permitted to sort semen using their intimate knowledge of XY's equipment and protocols without paying royalties to XY and in competition with other licensees in China, Canada or elsewhere who do pay royalties. The injunction is an appropriate remedy, both mandatory and prohibitory.

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The plaintiff's mandatory injunction is sought to deliver or destroy under oath confidential information of XY which is in the hands of the defendants. The defendants have no right to possess such information and indeed do not assert they do. The injunction does no more than hold JingJing and its employees and related companies who had access to the bargain struck under the CLA. [At paras. 328-29.]

103 The judge rejected the defendants' argument that XY's technology was in the public domain — an argument based on an answer given by Mr. Evans in his (public) testimony at trial. This answer, the judge said, had been taken entirely out of context: Mr. Evans was not referring to the information about which he later testified, *in camera*, at trial. As well, the judge rejected Mr. Zhu's evidence that semen could be sorted by the defendants without XY's confidential information. Aside from the fact that Mr. Zhu was not found to be credible, this evidence was contrary to the "detailed and credible evidence" of Mr. Gilligan and Mr. Evans. (Para. 337.)

104 In the result, the Court granted the injunction in the terms proposed by XY. This part of the Court's order is reproduced as Schedule II to these reasons.

105 Mr. Zhu complains on his appeal about many detailed aspects of the injunction, but the main thrust of his argument is that the definition of "Confidential Information" contained in Appendix A encompasses information that has been made publicly available (by the publication of research or through patent applications). Thus it fails to distinguish between that information and information that is truly confidential. On this view, the trial judge was "required to examine the circumstances of XY's claim for confidentiality and [to] make an independent determination as to whether the information was truly confidential such that the Court's protection of XY's information was required indefinitely".

106 The starting point for the relevant definition of "Confidential Information" in this case must be the terms of the CLA. As the trial judge noted at para. 204, the terms of any contract between the parties are relevant to the availability of a claim (and therefore, remedy) for breach of confidence. As seen above, s. 3.10 of the Agreement *excepted* information that is or becomes generally available to the public other than as a result of a disclosure by the recipient party, and information that was known by the recipient party "on a non-confidential basis and not in contravention of applicable law or confidentiality or other similar agreement prior to disclosure to [JingJing] by [XY]." Obviously, this would include published research and patent applications, and I did not understand XY to argue to the contrary.

107 It is not appropriate, however, for a court to refer to all such patent applications and public research in the terms of an order. While recognizing that any injunction must be clear and enforceable, it seems to me that any question of overbreadth in this instance could have been avoided by the incorporation of the exceptions listed in s. 3.10 of the CLA quoted above. Aside from this exception, JingJing agreed to keep the technology confidential, and for its part, XY took every precaution to see that the licensee did so. As the trial judge observed, the confidentiality of the technology was also supported by the standard terms and conditions of DakoCytomation's contract with JingJing for the sale of SX cytometers. (Para. 208.)

108 The trial judge analyzed the three different types of confidential information identified in this case, beginning at para. 209. He accepted Mr. Evan's evidence concerning the components of the SX cytometer that were confidential. Mr. Evans' *in camera* testimony confirmed that licensees are not even able to modify or add to most of the cytometer components. The Court accepted that the "protocols", or information regarding the use of the SX cytometer, given to Dr. Remillard had also been confidential. The Court continued:

> As Mr. Gilligan explained in his testimony, although much of the information contained in the report had been published, the summary prepared by XY was "the entirety of our field work up to [2003] ... [p]ublished and unpublished, which gives anybody who holds it a very good understanding of what we do or don't know so far, published or unpublished." In keeping with the principle from *Saltman Engineering* referred to in dissent by Sopinka J. in *Lac Minerals*, it is clear the people at XY had used their brains in creating XY's protocols based on published and unpublished research and experiments and had produced something that could only be produced by having

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> gone through such a process. As such, it is clear that the information contained in the protocols was confidential and the plaintiff's evidence that the protocols were conveyed in confidence has not been undermined. [At para. 215; emphasis added.]

109 Finally, with respect to XY's patent applications pending in China, the Court noted that applicants are normally reluctant to disclose their application information because it enables competitors to challenge the applications. (Para. 216.) Indeed, that is exactly what happened here: JingJing challenged XY's Chinese patent applications in breach of an express prohibition, stated to be effective during the term of the license. (Para. 224.)

110 The terms of the injunction and specifically its definitions of "Proprietary Rights" and "Patent Rights" and "Trademark Rights" essentially track the corresponding definitions in the CLA. As already noted, they were subject to the exceptions stated in s. 3.10. The definition of "Patent Rights" becomes relevant only because "Confidential Information" is defined to include "Improvements to the Confidential Information *made by the defendants*"; the definition of "Improvements" contains the term "XY's Technology"; XY's Technology is defined to include "Proprietary Rights"; and that term in turn includes "Patent Rights". Following this chain, I agree with Mr. Wilson that patents and trademarks *per se* are not captured by the order; rather it is improvements "*made by the defendants*, including but not limited to all research and development regarding the use of sexed semen *by any of the defendants* internally or with the assistance of third parties such as, but not limited to, [the] Abbotsford Veterinary Clinic." In these circumstances, I do not agree with Mr. McFee's submission that the order operates to prevent the use of information that has been made public as a result of patent applications by *persons other than the defendants*. (Emphasis added.)

111 Mr. Zhu also objects that the final clause (which I have labelled clause "(f)") of Appendix A to the order prevents him from using "the research and development of the defendants within the Field of Use and outside the Field of Use with respect to *in vivo* embryos and any other matters using sexed semen". The term "Field of Use" is defined broadly — too broadly, according to Mr. Zhu. In his submission, it precludes him from pursuing businesses that involve the production of embryos that are not dependent on XY's technology. The order prevents the defendants, for example, from purchasing sexed semen from another licensee of XY and then producing the resulting sexed embryos. Mr. Zhu testified that prior to the CLA, JingJing had engaged in such research and development without using XY's technology. (Para. 72.)

112 XY responds that the trial judge expressly did not find this evidence persuasive. (Para. 337.) There was no evidence that Mr. Zhu had any "legitimate business" in the same field as XY that does not rely on XY's technology. Thus, it is said, "[t]here is nothing unjust about now constraining his behaviour to correspond with the bargain that first gave him access to the sexed semen technology, which he agreed was 'one of the world's most promising biotechnologies'".

113 XY is understandably distrustful of Mr. Zhu and wants to cast its net widely so as to avoid having to re-litigate the confidentiality of its information at a later date should Mr. Zhu re-enter the business of producing embryos or otherwise using sexed semen. Nevertheless, XY's rights do not go so far as to entitle it to demand that Mr. Zhu never enter or re-enter that business. He and his companies, however, may not use or build on XY's technology to do so. It is not clear to me whether paragraph (f) was specifically referred to in argument before the trial judge, but in my respectful view, it is overly broad. I regard paragraphs (d) and (e) as sufficient to capture the defendants' future use of XY's technology, especially in light of the definition of "Improvements".

114 I would therefore allow Mr. Zhu's appeal to the extent of deleting what I have denoted as paragraph (f) of Appendix A to the order, and incorporating the exceptions listed in s. 3.10 of the CLA, with appropriate changes in nomenclature. In all other respects, I would dismiss the appeal concerning the terms of the permanent injunction.

Calculation of Damages

The 50% Discount

115 Finally, Mr. Zhu challenges certain aspects of the trial judge's calculation of damages (see para. 16 above). First, it is said the judge erred in neglecting to give effect to a 50% discount, agreed to by XY in a letter agreement dated June

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5, 2006, from the royalty payable by JingJing on the sale of sexed embryos. This discount was to continue for one year from the date of the letter agreement. Mr. Wilson responds that this matter was not raised below in connection with the quantum of damages and that had it been raised, XY would have adduced evidence that it was induced by JingJing's fraud to agree to the discount. XY refers in particular to evidence that JingJing had lied to it from the beginning regarding its embryo production, which it reported as 'nil' for the first few months and underreported thereafter. I agree with XY that this matter should have been raised below, and that it would be prejudicial now to permit JingJing to claim the discount.

Sale of AI Straws

116 In calculating the damages, the trial judge stated at para. 294 of his reasons that there was "no dispute" that royalties of $6 per AI straw on 195,148 straws was payable. Counsel for Mr. Zhu says that the matter was and is very much in dispute.

117 The figure of 195,148 AI comes from the addition of two columns in Ms. Tang's records which were tendered in evidence by XY, one of which showed "AI straw produced/service render" and the other of which showed "Produced/ service render for other purpose (R & D)". Royalties were payable to XY only on AI straws that were "used". Counsel for Mr. Zhu did not refer us to any other records in support of his contention that Ms. Tang's figure was overstated. He pointed us only to a letter from JingJing's former counsel to Mr. Wilson in November 2008 in which $244,542 (USD) was offered by JingJing in respect of sexed semen calculated to September 30, 2008. It is not clear how the monetary figure was reached and Mr. McFee did not refer to any other reliable records to clarify the number of AI straws that were sold, as opposed to produced.

118 In these circumstances, I would not fault the trial judge for adding together the two columns in Ms. Tang's records to reach the total number of AI straws on which to calculate damages.

Expert Report

119 Last, Mr. Zhu asserts that the trial judge erred in excluding from evidence an expert report proffered by the defendants concerning the fair market value of IVF embryos in China. This figure was relevant to the calculation of royalties payable before and after January 2007 on such embryos, discussed by the trial judge at paras. 278-96 of his reasons. The judge began his discussion by noting that because JingJing had not produced the records that could have shown the number of embryos used in China, it was necessary for the Court to infer the appropriate number on the evidence before it. At para. 285, the judge found that taking all the evidence he had into account, the figure of 500,000 embryos for the period before January 2007 and 150,000 in the period thereafter could be fairly inferred.

120 As for the fair market value of the embryos, XY adduced expert evidence from Dr. Gordon MacDonald, who testified that *un*sexed IVF embryos (generally sold at half the price of sexed embryos) sold at between $60 and $75 USD. The judge found that this evidence 'made sense' and was consistent with other evidence regarding fair market value. (Para. 290.) Although the plaintiff's claim that the average value before January 2007 was $135 and $150 after January 2007, the Court settled on a value of $125 before January 2007 and $150 thereafter.

121 On February 6, 2011, three months into the trial and the first day of the recommencement of the trial after a break, JingJing sought to tender an expert report from Dr. Richard Vanderwal, a doctor in veterinary medicine who practices in Abbotsford. His opinion was tendered in response to Dr. MacDonald's opinion. In explaining his lateness in tendering Dr. Vanderwal's evidence, counsel for JingJing advised the Court that his client had previously arranged for a report from an expert who lives in China, Zhu Yu Lin. The trial judge recounted in his ruling:

> Questions arose about the authenticity of the report. Mr. Zhu then advised the defendants that he refused to come to Vancouver to appear in court. There is a suggestion that the plaintiff may have had a role in Mr. Zhu's refusal. There is no cogent evidence that this is the case and I draw no such inference.

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> The evidence is that after October 20 th , 2010, counsel for the defendant canvassed ten people as potential experts. Each refused based on unavailability, lack of relevant expertise or existing relationships with one of the parties to the litigation.
>
> The defendant tried to contact Dr. Vanderwal on November 14th. Ms. Prestegar has deposed that these efforts did not produce any results. Those efforts continued until prior to the holiday period in late December.
>
> On January 25th, counsel for the defendants discussed the matter with Mr. Vanderwal and confirmed that he would prepare a report. It was obtained by the defendant on Sunday, February 6th, 2011, and served on plaintiff's counsel the same afternoon or evening.

122 The judge noted that under R. 11-7(6), the Court may allow an expert to provide a responsive expert's report "at trial" if non-compliance with the general time-limit of 42 days before trial is unlikely to cause prejudice *or* the interests of justice require it. The judge was not persuaded that either of these circumstances arose. In his analysis:

> Where circumstances beyond the defendants' control deprive them of an expert witness, the court will look favourably on accommodating this difficulty. The substantial prejudice to the plaintiff will not necessarily be a bar to the exercise of discretion. The interest of justice is often the overriding factor. But that is only where a party is [assiduous] in making efforts to locate a new witness. I am unable to say this is the case here. I infer that by early January, the defendant had decided not to pursue the search further. It was only three weeks later that these efforts were renewed and were successful.
>
> In the circumstances, I am not exercising my discretion and the report is excluded.

123 Mr. McFee on behalf of JingJing submits that the Court here erred in failing to consider the "interests of justice" separately from prejudice under para. (b) or due diligence under para. (a) of R. 11-7(6). On this point, he relied on *A. (C.) v. C. (J.W.)*, [1996] B.C.J. No. 3055 (B.C. S.C. [In Chambers]) at para. 12 and on *Perry v. Vargas*, 2012 BCSC 1537 (B.C. S.C.). At para. 20 of *Perry v. Vargas*, it was said that by virtue of R. 11-7(6)(c), the Court retains a residual discretion to dispense with the other requirements of R. 11 in the interests of justice. In Mr. McFee's submission, the trial judge was required to consider the interests of justice separate from prejudice and due diligence, and in so doing to consider whether an adjournment of the trial or other steps could be granted to delay the cross-examination of Dr. Vanderwal. As a result of proceeding on the basis of the plaintiff's expert alone, counsel suggests that the judge ultimately used incorrect figures for the fair market values of embryos in China in his calculation of XY's damages.

124 I am not persuaded that the trial judge so erred. He noted, correctly, that his discretion was "only to be exercised where there is prejudice or the interests of justice require it." As I read his reasons, he considered that prejudice and the defendants' diligence were relevant to the interests of justice. It is difficult to argue with this proposition. I respectfully adopt the observations of the Court in *Perry v. Vargas*:

> In my view the discretion provided for in R.11-7(6)(c) must be exercised sparingly, with appropriate caution, and in a disciplined way given the express requirements contained in Rules 11-6 and 11-7. That is, the "interests of justice" are not a reason to simply excuse or ignore the requirements of the other Rules. There must be some compelling analysis why the interests of justice require in a particular case the extraordinary step of abrogating the other requirements of the *Supreme Court Civil Rules*. None was provided. [At para. 22.]

125 Given the deference due to a discretionary decision of this kind, I would not interfere with the trial judge's ruling in this case. I take additional comfort from the fact that the proposed expert was in fact the veterinarian in Abbotsford with whom JingJing had an important business relationship, and was thus an expert whose independence and impartiality in this case might well have been suspect.

126 I would dismiss the appeal concerning the calculation of damages.

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Special Costs

127 As far as the judge's order for special costs is concerned, I see no basis to interfere with that order and indeed I find it was fully justified in light of the defendants' conduct of this litigation.

Disposition

128 In summary, I would allow the appeals to the limited extent set out below:

- I would allow XY's appeal to the extent that I would set aside para. 9 of the trial judge's Order and substitute therefor:

    9. The plaintiff's claims against International Newtech Development Incorporated, IND Lifetech Group Ltd., IND Lifetech (U.S.A.) Incorporated, IND Lifetech (USA) Inc., IND Lifetech (Qingdao) Co. Ltd., IND Lifetech (Zouping) Co. Ltd. and IND Embryontech Inc. for the torts of deceit, civil conspiracy and inducing breach of contract are dismissed; but the claims in respect of unjust enrichment against the said corporate defendants shall be remitted to the Supreme Court of British Columbia for retrial. The plaintiff's claims against Zhen Hong Liu are dismissed in their entirety.

  (XY has confirmed it seeks no order against "IND Lifetech Co. Ltd.," or Shanghai JingJing Biotech Co. Ltd.)

- I would allow the corporate defendants' appeal to the extent that I would add to Appendix A to the order, following subparagraph (vii) of paragraph (e) thereof, the following:

    Provided that Confidential Information shall not include information that

    i. is or becomes generally available to the public other than as a result of a disclosure by any of the defendants;

    ii. becomes available to any of the defendants on a nonconfidential basis and not in contravention of applicable law from a source, other than the plaintiff herein or one of its officers, directors, partners, employees, independent contractors, agents, or licensees ("Representatives") not bound by a confidential relationship with the plaintiff or by a confidentiality or other similar agreement;

    iii. can be proven was known by any of the defendants on a non-confidential basis and not in contravention of applicable law or confidentiality or other similar agreement prior to disclosure to any defendant by the plaintiff.

And I would delete paragraph (f) of Schedule A to the Order.

If counsel are of the view that the foregoing terms of this order do not properly reflect this court's intentions as inferred from these reasons, or that they create a difficulty of which the Court may not be aware, they should advise the Registrar in writing within 20 days.

129 We are indebted to all counsel for their able arguments.

***Chiasson J.A.*:**

I Agree:

***D. Smith J.A.*:**

I Agree:

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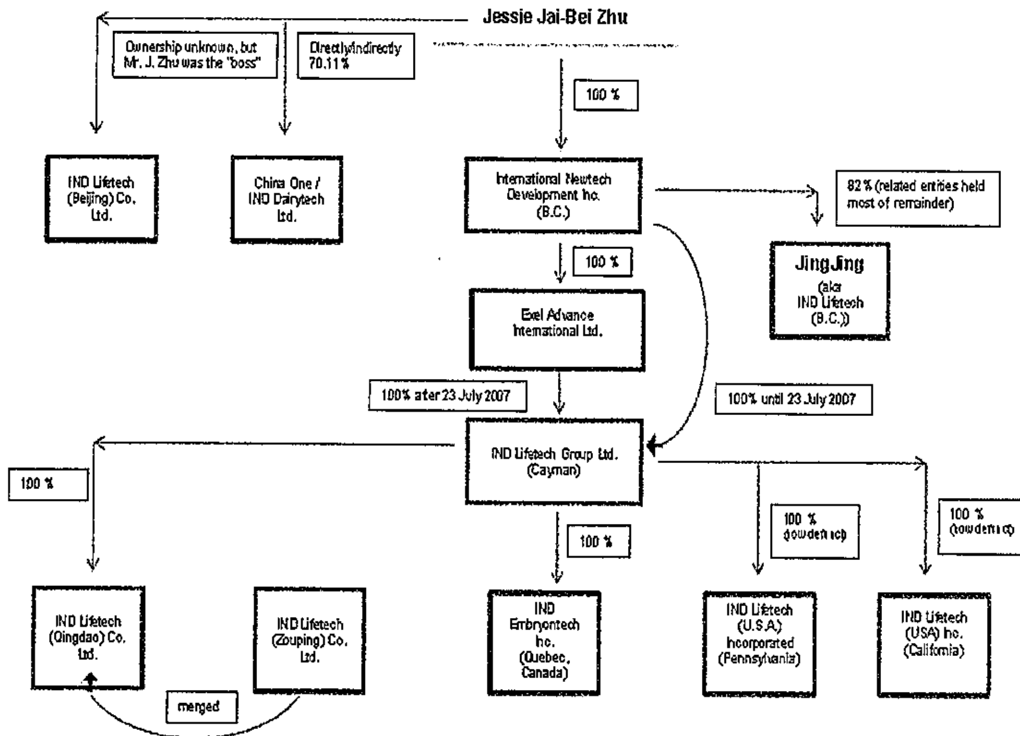
Schedule 1 — Corporate Chart



Schedule II

(Part of Order after Trial of the Supreme Court of British Columbia):

Mandatory and Prohibitory Injunction

12. The plaintiff is entitled to a prohibitory injunction to protect the plaintiff's Confidential Information including all Improvements;

13. The plaintiff is also entitled to a mandatory injunction to deliver up the Confidential Information and Improvements made possible by or because of access to the plaintiff's technology;

14. In this Order, the term "*Confidential Information*" has the meaning set out in Appendix "A" attached hereto;

15. The defendants JingJing, Jesse Jia-Bei Zhu, Selen Zhou, Tang Jin, and Shu Xi Wang and each of them (including by themselves, or by their directors, officers, agents, employees, servants, affiliates, joint venturers, successors, assigns, subsidiaries or related companies, and all those over whom they exercise control, directly or indirectly) are restrained from using the Confidential Information, for any purpose or to any extent, and are restrained from communicating, transferring, distributing, selling, publishing, leasing, licensing or in any other way or by any other means disclosing the Confidential Information to any person or for any purpose; and

16. Within 14 days from the date of this order, namely on or before March 16, 2012, the defendants JingJing, Jesse Jia-Bei Zhu, Selen Zhou, Tang Jin, and Shu Xi Wang and each of them, shall deliver up to the plaintiff or its designate any and all Confidential Information in their possession, power or control.

Appendix "A" to the Order After Trial of the Supreme Court of British Columbia

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In this Order After Trial "*Confidential Information*" means:

(a) The following components of the Dako SX Mo-Flo Cytometer, including their configuration individually and in relation to each other and other components of the cytometer:

(i) the PMT (photomultiplier tube) controller;

(ii) the nozzle assembly;

(iii) the beam-shaping optics;

(iv) the detector system;

(v) laser beam steering towers, stages and optics;

(vi) the Summit Workstation hardware and Summit software with Cytrack;

(vii) the pulsed laser as configured for the SX cytometer;

(viii) the illumination chamber;

(ix) the front door rail;

(x) the strobe assembly; and

(xi) the pinhole strip;

(b) XY's protocols, as set out in document no. XY015125-175, entitled "XY, Inc. Protocols — Confidential — September 2005" and document no. XY016423-502, entitled "XY, Inc. Protocols — Confidential — March 2006";

(c) The technical data and processes contained in XY's report entitled "Confidential Information for the Purpose of Evaluating a MoFlo SX Sperm Sorting Facility in Canada", document no. XY001229-001237;

(d) All other information and techniques imparted from XY during training or otherwise to any of the defendants and their employees relating to the use and operation of SX cytometers;

(e) Improvements to the Confidential Information made by the defendants, including but not limited to all research and development regarding the use of sexed semen by any of the defendants internally or with the assistance of third parties such as, but not limited to, Abbotsford Veterinary Clinic; and where:

(i) Improvements means namely all know-how, processes, operations, methods, masks, codes, programs, designs, copyrights, patents, patent applications, or other intellectual property rights or other information created, obtained, or developed by either XY or any licensee of XY or JingJing whether through their own efforts or those of any independent contractor, employee, affiliate, or subsidiary, or directly or indirectly with any third party, based upon or derived from XY's Technology, in whole or in part;

(ii) XY's Technology means any and all Proprietary Rights or confidential information, trade secrets, know-how, technical data, masks, code, programs, designs, processes, methods, operations, innovations or inventions, whether or not patented, and any patents, patent applications, copyrights, or other intellectual property of any kind that XY, now or hereafter, owns, controls, licenses, or has an interest in;

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(iii) Proprietary Rights with respect to XY's Technology means the collection of all Patent Rights, Trademark Rights, Trade Secret Rights, and Copyright Rights, or other rights which are or may be asserted as protectable under the laws of the United States or the laws of any foreign county;

(iv) Patent Rights with respect to XY's Technology means all rights which are or may be asserted as protectable by license or under the patent laws of the United States or the patent laws, or similar laws, of any foreign country or region, including, but not limited to, any patent applications or grants of patent along with any division, substitution, continuation, continuation-in-part, continued prosecution, or other patent application(s) thereof filed in the United States, under international treaty or agreement, or in any foreign country or region, and all patents, utility models, inventor's certificates, or other similar rights which may be granted thereon and any reissues or extensions thereof, and specifically includes, but is not limited to, those patent rights to United States Patent No. 5,135,759 pursuant to the license agreement with the United States Department of Agriculture, Agricultural Research Service ("USDA License") subject to the reservation of rights therein, including reservation by the Agricultural Research Service of an irrevocable, nonexclusive, nontransferable, royalty-free, license to practice the licensed patent throughout the world by or on behalf of the United States Government and on behalf of any foreign government pursuant to any existing or future treaty or agreement to which the United States is a signatory, and the right to engage in research, either alone or with third parties, with respect to the claimed inventions;

(v) Trademark Rights with respect to XY's Technology means all rights, whether registered or not, which are or may be asserted as protectable by license or under trademark, unfair competition, trade dress, anti-dilution, or similar laws of the United States, or any state, or any foreign country or region;

(vi) Trade Secret Rights with respect to XY's Technology means all trade secrets, confidential information, and know-how which are or may be asserted as protectable by license or under the trade secret, confidentiality, or unfair competition laws of any state, or under similar laws of any foreign country or region;

(vii) Copyright Rights with respect to XY's Technology means all rights, whether registered or not, which are or may be asserted as protectable under the copyright laws of the United States or the copyright laws of any foreign country.

(f) Specifically including but not limited to the research and development of the defendants within the Field of Use and outside the Field of Use with respect to *in vivo* embryos and any other matters using sexed semen:

(i) (Field of Use means the collection and preparation of cattle semen, the separation of spermatozoa in such cattle semen into sex-selected subpopulations of cattle spermatozoa based upon the presence of an X-chromosome or a Y-chromosome, use of such sex-selected subpopulations of cattle spermatozoa for in-vitro fertilization of cattle oocytes, the production of sex-selected cattle embryos utilizing in-vitro fertilization, cryogenic storage of such cattle semen, such sexselected subpopulations of cattle spermatozoa, and such sex selected cattle embryos produced utilizing in-vitro fertilization)

Appeals allowed in part; cross-appeal dismissed.

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Court File No. CV-16-11549-00CL

IN THE MATTER OF THE COMPANIES' CREDITORS ARRANGEMENT ACT, R.S.C. 1985, C. c-36, AS AMENDED, AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF URBANCORP (WOODBINE) INC. AND URBANCORP (BRIDLEPATH) INC., THE TOWNHOUSES OF HOGG'S HOLLOW INC., KING TOWNS INC., NEWTOWNS AT KINGTOWNS INC. AND DEAJA PARTNER (BAY) INC. (COLLECTIVELY, THE "APPLICANTS") AND IN THE MATTER OF TCC URBANCORP (BAY) LIMITED PARTNERSHIP

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Proceedings Commenced at Toronto

JOINT BOOK OF AUTHORITIES OF THE FUNCTIONARY AND TERRA FIRMA CAPITAL CORPORATION

DENTONS CANADA LLP
77 King Street West, Suite 400
Toronto, Ontario M5K 0A1
Fax: 416-863-4592

Kenneth Kraft (LSO No. 31919P)
Tel: 416-863-4374
Email: kenneth.kraft@dentons.com

Neil Rabinovitch (LSO No. 33442F)
Tel: 416-863-4656
Email: neil.rabinovitch@dentons.com

Lawyers for the Moving Party, Guy Gissin the Israeli Court-appointed functionary officer and foreign representative of Urbancorp Inc.

THORNTON GROUT FINNIGAN LLP
3200-100 Wellington Street West
TD Centre, Box 329
Toronto, ON M5K 1K7

John T. Porter (LSO No. 23844T)
Tel: (416) 304-0778
Fax: (416) 304-1313
Email: jporter@tgf.ca

Counsel for Terra Firma Capital Corporation