Court of Appeal File No: M49270
Court File No. CV-16-11389-00CL

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 TORONTO MANAGEMENT INC., URBANCORP TORONTO MANAGEMENT INC., URBANCORP (ST. CLAIR VILLAGE) INC., URBANCORP (PATRICIA) INC., URBANCORP (MALLOW) INC., URBANCORP (LAWRENCE) INC., URBANCORP DOWNSVIEW PARK DEVELOPMENT INC., URBANCORP (952 QUEEN WEST) INC., KING RESIDENTIAL INC., URBANCORP 60 ST. CLAIR INC., HIGH RES. INC., BRIDGE ON KING INC. (COLLECTIVELY, THE "APPLICANTS") AND THE AFFILIATED ENTITIES LISTED IN SCHEDULE "A" HERETO

BOOK OF AUTHORITIES OF SPEEDY ELECTRICAL CONTRACTORS LTD.
(Motion For Leave to Appeal)

July 12, 2018

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TO: **SERVICE LIST**

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Tab 1

2016 CarswellOnt 21662
Ontario Court of Appeal

4519922 Canada Inc., Re

2016 CarswellOnt 21662, 277 A.C.W.S. (3d) 239

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 4519922 Canada Inc.

Hoy A.C.J.O., Lauwers, Benotto JJ.A.

Heard: September 16, 2016
Judgment: September 22, 2016
Docket: CA M46647

Proceedings: refusing eave to appeal *4519922 Canada Inc., Re* (2016), 37 C.B.R. (6th) 272, 2016 CarswellOnt 9518, 2016 ONSC 3681, Newbould J. (Ont. S.C.J. [Commercial List])

Counsel: Counsel — not provided

Subject: Civil Practice and Procedure; Insolvency

MOTION by creditor for leave to appeal judgment reported at *4519922 Canada Inc., Re* (2016), 2016 ONSC 3681, 2016 CarswellOnt 9518, 37 C.B.R. (6th) 272 (Ont. S.C.J. [Commercial List]), ordering creditor and others to sign indemnity and release to indemnify law firm against tax liability that might accrue as result of cost award made in litigation.

Per curiam:

1 This is a motion for leave to appeal under s. 13 of the *Companies' Creditors Arrangement Act*, R.S.C., c. C-36.

2 The moving party, FCA Canada Inc. ("FCA"), seeks leave to appeal an order directing it to sign an agreement indemnifying the responding party, Fishman Flanz Meland Paquin LLP ("FFMP"), from any tax liability it might incur in distributing a cost award arising from a successful professional negligence claim against the accounting firm formerly known as Coopers & Lybrand LLP ("CLCA").

3 The FCA submits that the indemnity is inconsistent with an earlier, "unconditional" undertaking in which FFMP stated that it would pay FCA is *pro rata* share of the cost award funds. The supervising judge rejected this submission and ordered FCA to sign the indemnity as a precondition to FFMP paying out its funds. FCA argues that in so ordering, the supervising judge erred in law and in fact. It claims that leave to appeal is warranted according to the strict criteria set out in the court's jurisprudence:

(a) whether the proposed appeal is *prima facie* meritorious or frivolous;

(b) whether the point on the proposed appeal is of significance to the practice;

(c) whether the point on the proposed appeal is of significance to the action; and

(d) whether the proposed appeal will unduly hinder the progress of the action.

See, for e.g.: *Nortel Networks Corp., Re*, 2016 ONCA 332, 130 O.R. (3d) 481 (Ont. C.A.), leave to appeal requested [2015 CarswellOnt 7072 (Ont. S.C.J. [Commercial List])]; *Stelco Inc., Re* (2005), 75 O.R. (3d) 5 (Ont. C.A.), at para. 24; *Timminco Ltd., Re*, 2012 ONCA 552, 2 C.B.R. (6th) 332 (Ont. C.A.), at para. 2.

4 We are satisfied that FCA has failed to establish any of these requirements.

5 This is a highly fact-specific dispute that involves questions within the broad discretion of the supervising judge. We are not persuaded that the proposed appeal is meritorious, or that it has import for the practice as a whole. Meanwhile, a final distribution to CLCA's creditors awaits the resolution of this claim. An appeal would unduly hinder a definitive end to this long-delayed litigation.

6 Accordingly, we dismiss the motion for leave to appeal.

7 The responding party shall be entitled to its costs of this motion, fixed in the amount of $1,500.

Motion dismissed.

End of Document

Tab 2

2016 ONCA 749
Ontario Court of Appeal

SNMP Research International Inc. v. Nortel Networks Corp.

2016 CarswellOnt 15976, 2016 ONCA 749, 271 A.C.W.S. (3d) 699, 41 C.B.R. (6th) 174

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

And in the matter of a plan or arrangement of Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation and Nortel Networks Technology Corporation

SNMP Research International Inc. and SNMP Research Inc. (Claimants) and Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation and Nortel Networks International Corporation and Nortel Networks Technology Corporation (Debtors)

Alexandra Hoy A.C.J.O., M.L. Benotto, Grant Huscroft JJ.A.

Judgment: October 14, 2016
Docket: CA M46504

Counsel: Counsel — not provided

Subject: Insolvency

MOTION by claimants for leave to appeal from judgment granting partial summary judgment to debtor and dismissing claimants' profits claim

Per curiam:

1 This motion for leave to appeal arises out of the Nortel insolvency.

2 SNMP Research International Inc. and SNMP Research Inc. (collectively, "SNMP"), licenced its software products to Nortel to use in its computer networks. Nortel's use of the software was governed by a 1999 licence agreement that provided, among other things, that Nortel would keep SNMP's source code strictly confidential. When Nortel's assets were sold during the *CCAA* proceedings beginning in 2009, some of SNMP's source code was transferred along with those assets. Nortel acknowledged that it was not authorized to provide source code to anyone, and that in doing so it breached its licence agreement with SNMP. SNMP sued Nortel, advancing two claims: one for disgorgement of profits attributable to the unauthorized transfer of SNMP's intellectual property ("the profits claim"), and one for damages for breach of contract, copyright infringement and breach of confidence ("the damages claim"). The profits claim is valued at $86 million. The damages claim is for a comparatively much smaller amount.

3 The supervising judge granted partial summary judgment to Nortel and dismissed the profits claim. He ordered that the damages claim be held in abeyance for six months pending ongoing discovery in a parallel U.S. proceeding.

4 In dismissing the profits claim, the supervising judge held that while Nortel had infringed SNMP's copyright, SNMP failed to show that Nortel profited from the unauthorized transfer of SNMP's intellectual property. Instead, the evidence established that the companies that bought Nortel's assets knew they were not buying SNMP's software and would instead have to negotiate licencing fees with SNMP directly.

5 SNMP now seeks leave to appeal.

6 Leave to appeal is granted sparingly in *CCAA* proceedings and only where there are serious and arguable grounds that are of real and significant interest to the parties. In considering whether leave should be granted, the court will consider:

(a) whether the proposed appeal is *prima facie* meritorious or frivolous;

(b) whether the point on the proposed appeal is of significance to the practice;

(c) whether the point on the proposed appeal is of significance to the action; and

(d) whether the proposed appeal will unduly hinder the progress of the action.

See, for e.g.: *Stelco Inc., Re* (2005), 75 O.R. (3d) 5 (Ont. C.A.), at para. 24; *Timminco Ltd., Re*, 2012 ONCA 552, 2 C.B.R. (6th) 332 (Ont. C.A.), at para. 2.

7 We conclude that leave should not be granted.

8 On the first factor, the proposed appeal turns on the supervising judge's findings of fact about the sufficiency of the evidence SNMP marshalled to oppose Nortel's motion for summary judgment. Those findings are entitled to deference and cannot be disturbed on appeal absent palpable and overriding error: *Hryniak v. Mauldin*, 2014 SCC 7, [2014] 1 S.C.R. 87 (S.C.C.), at para. 81. We see no such error in the supervising judge's reasons.

9 Our conclusion on the second factor follows from our conclusion on the first. Contrary to SNMP's submissions, the proposed appeal turns on the particular facts of this case and does not raise broader issues about the intersection of copyright law and insolvency law. The supervising judge's decision does no more than decide that in this case, on these facts, SNMP did not meet its burden under s. 35(2) of the *Copyright Act*, R.S.C. 1985, c. C-42, to prove that Nortel derived revenues from its infringement of SNMP's copyright. The proposed appeal does not raise issues of significance to the practice.

10 On the third factor, we observe that this court very recently refused leave to appeal in another Nortel matter, one which addressed the allocation of some $7.3 billion in proceeds from the sale of Nortel's assets: *Nortel Networks Corp., Re*, 2016 ONCA 332, 130 O.R. (3d) 481 (Ont. C.A.), leave to appeal to S.C.C. requested [2016 CarswellOnt 14117 (S.C.C.)]. In that case, the court observed that even if the allocation issue was significant to the *CCAA* proceeding, that factor, standing alone, was insufficient to warrant granting leave. The court observed, at para. 95: "To perhaps state the obvious, typically parties tend to seek leave to appeal a decision that is of significance to an action."

11 Finally, this motion for leave has to be considered in the context of the Nortel litigation as a whole. As this court emphasized in the allocation decision, these proceedings have dragged on for several years, to the detriment of individuals and businesses awaiting a resolution. The fact that this is a liquidation rather than a restructuring does not render the delay immaterial. Given our conclusions on the other three leave factors, we are not satisfied that a further delay is justified in these circumstances.

12 For these reasons, the motion for leave to appeal is dismissed.

13 The responding party shall be entitled to its costs of the motion, fixed at $1,500.

Motion dismissed.

End of Document

Tab 3

2016 ONCA 332
Ontario Court of Appeal

Nortel Networks Corp., Re

2016 CarswellOnt 6785, 2016 ONCA 332, 130 O.R. (3d) 481,
265 A.C.W.S. (3d) 834, 348 O.A.C. 131, 36 C.B.R. (6th) 1

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 Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation Application under the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

Alexandra Hoy A.C.J.O., R.A. Blair, S.E. Pepall JJ.A.

Judgment: May 3, 2016
Docket: CA M45307, M45309, M45310 M45311, M45312, M45313

Proceedings: refusing leave to appeal *Nortel Networks Corp., Re* (2015), 27 C.B.R. (6th) 175, 2015 CarswellOnt 7072, 2015 ONSC 2987, Newbould J. (Ont. S.C.J. [Commercial List]); and refusing leave to appeal *Nortel Networks Corp., Re* (2015), 27 C.B.R. (6th) 51, 2015 ONSC 4170, 2015 CarswellOnt 10304, Newbould J. (Ont. S.C.J. [Commercial List])

Counsel: Sheila Block, Scott A. Bomhof, Andrew Gray, Adam M. Slavens, Jeremy Opolsky, for Moving parties, U.S. Debtors(1)
Richard B. Swan, S. Richard Orzy, Gavin H. Finlayson, for Moving party, Ad Hoc Group of Bondholders
David R. Byers, Daniel S. Murdoch, for Moving party, Conflicts Administrator of Nortel Networks S.A.
Shayne Kukulowicz, Michael Wunder, Ryan Jacobs, Geoffrey Shaw, Jane Dietrich, for Moving party, Official Committee of Unsecured Creditors of Nortel Networks Inc. et al.
Andrew Kent, Brett Harrison, Laura Brazil, for Moving party, Bank of New York Mellon as Indenture Trustee
Steven L. Graff, Ian Aversa, Miranda Spence, for Moving party, Nortel Trade Claims Consortium
Michael E. Barrack, D.J. Miller, John L. Finnigan, Michael S. Shakra, Andrea McEwan, for Responding parties, Board of the Pension Protection Fund and Nortel Networks U.K. Pension Trust Ltd.
Benjamin Zarnett, Jessica Kimmel, Peter Ruby, Peter Kolla, for Responding party, Monitor, Ernst & Young Inc.
Kenneth Kraft, John Salmas, for Responding party, Wilmington Trust, National Association
Derrick Tay, Jennifer Stam, for Responding parties, Canadian Debtors(2)
Kenneth Rosenberg, Lily Harmer, Massimo Starnino, for Responding party, Superintendent of Financial Services as Administrator of the Pension Benefits Guarantee Fund
Mark Zigler, Ari Kaplan, for Responding parties, Former Employees of Nortel and LTD Beneficiaries
Arthur O. Jacques, Paul Steep, Byron Shaw, for Responding party, Canadian Creditors' Committee
Barry E. Wadsworth, for Responding party, CAW-Canada
Matthew P. Gottlieb, Matthew Milne-Smith, for Responding parties, Joint Administrators of the EMEA Debtors(3) other than Nortel Networks S.A.

Subject: Contracts; Estates and Trusts; Evidence; Insolvency; Intellectual Property; International; Property

MOTIONS for leave to appeal from decisions reported at *Nortel Networks Corp., Re* (2015), 2015 ONSC 2987, 2015 CarswellOnt 7072, 27 C.B.R. (6th) 175 (Ont. S.C.J. [Commercial List]) and *Nortel Networks Corp., Re* (2015), 2015

ONSC 4170, 2015 CarswellOnt 10304, 27 C.B.R. (6th) 51 (Ont. S.C.J. [Commercial List]), regarding allocation of proceeds of sale of debtor's assets.

***Per curiam*:**

A. Introduction

1 January 14, 2009 was not a good day. At that time, Nortel Networks Corp. ("NNC") and the other Nortel Canadian Debtors filed for insolvency protection under the *Companies Creditors' Arrangement Act*, R.S.C. 1985, c. C-36 ("*CCAA*"). That same day, Nortel Networks Inc. ("NNI") and other U.S. Debtors filed voluntary petitions for relief under Chapter 11 of the U.S. *Bankruptcy Code*, 11 U.S.C. §§1101 - 1174, and other Nortel entities incorporated in Europe, the Middle East and Africa ("EMEA") were placed under administration in England by the High Court of England and Wales under the U.K. *Insolvency Act 1986*, c. 45. Shortly afterwards, courts in Canada and the United States approved a cross-border, court-to-court protocol that established procedures for the co-ordination of cross-border proceedings in Canada and the U.S.

2 More than seven years later, many Januarys have come and gone and these insolvency proceedings continue. During that time:

- more than 6,800 Nortel former employees or pensioners have died;
- well in excess of $1 billion has been incurred in costs; and
- Nortel's assets have been sold and some $7.3 billion [1] in sale proceeds have been placed in escrow (the "Lockbox Funds").

3 The leave motions now before this court arise from the joint trial dealing with the allocation of the Lockbox Funds. Newbould J. (the "trial judge) of Ontario's Superior Court of Justice (Commercial List) and Judge Gross of the U.S. Bankruptcy Court for the District of Delaware presided over the joint trial. [2] It was held over the course of six weeks. Each judge rendered separate decisions on May 12, 2015. Each concluded that the Lockbox Funds should be allocated on a *pro rata* basis among the various Nortel debtor estates. Although their analysis differed somewhat, the outcome was the same.

4 Appeal proceedings were initiated in Canada and the U.S. The moving parties were authorized to file their leave materials in the absence of an issued judgment on the basis that counsel would subsequently file the formal judgment. The formal judgment was issued on April 26, 2016 and filed with this court on April 27, 2016.

5 Before this court, the six moving parties, led by the U.S. Debtors, seek leave to appeal the trial judge's judgment pursuant to s. 13 of the *CCAA*. They submit that the trial judge made fundamental errors and that the proposed appeal is of significance to the practice of insolvency and to the parties, and will not delay the completion of the *CCAA* proceedings.

6 The responding parties, led by the Board of the Pension Protection Fund and Nortel Networks UK Pension Trust Limited ("UKPC"), submit that the record supports the trial judge's factual findings, which were integral to his analysis, including his findings that Nortel's assets were jointly created, that the Nortel group of companies operated on a fully-integrated global basis and that Nortel did not operate separate businesses in separate countries. In their submission, the proposed appeal is not *prima facie* meritorious. In addition, the remaining elements of the test for leave to appeal under the *CCAA* have not all been met.

7 After consideration of each of the factums [3] and other materials filed on the leave motions, we agree with the responding parties that the test for leave has not been met. For the reasons that follow, we dismiss the moving parties' motions for leave to appeal.

B. Genesis of Dispute

8 NNC was a publicly-traded Canadian corporation at the helm of a global networking solutions and telecommunications business, and the direct or indirect parent of more than 130 subsidiaries located in more than 100 countries. These companies were collectively referred to as the "Nortel Group" or "Nortel".

9 NNC was the successor to a long line of companies, headquartered in Canada, that date back to the founding of the Bell Telephone Company of Canada in 1883. NNC's principal, direct operating subsidiary was Nortel Networks Limited ("NNL"), also a Canadian company. NNL was the direct or indirect parent of operating companies located around the world. It owned 100 percent of the equity of each of the following entities: NNI, Nortel's operating company in the United States; Nortel Networks UK Ltd. ("NNUK"), Nortel's operating company in the United Kingdom; and, Nortel Networks (Ireland) Ltd. ("NN Ireland"), Nortel's operating company in Ireland. It also owned 91.17 per cent of the equity of Nortel Networks S.A. ("NNSA"), Nortel's operating company in France.

10 Following the insolvency filings, Nortel's initial plan was to downsize and carry on portions of the telecommunications business. However, by June 2009, the decision was made to liquidate Nortel's assets.

11 On June 29, 2009, an Interim Funding and Settlement Agreement ("IFSA") was approved by both the Canadian and American courts. Among other things, it addressed interim funding for NNL and the anticipated sales of Nortel's business lines and residual intellectual property ("IP"). The parties, consisting of the Canadian Debtors, the U.S. Debtors [4], and the EMEA Debtors [5], agreed to cooperate with the sales process and also agreed that the proceeds of sale would be held in escrow. The issue of allocation was deferred.

12 Under the IFSA, there would be no distribution out of escrow without "either (i) agreement of all of the Selling Debtors [6] or (ii) ... determination by the relevant dispute resolver(s) under the terms of the Protocol ... applicable to the Sale Proceeds". The parties were then to negotiate and attempt to reach agreement "on a protocol for resolving disputes concerning the allocation of Sale Proceeds from Sale Transactions (the "Interim Sales Protocol")". Despite numerous attempts at resolution, agreement on both an Interim Sales Protocol and allocation proved to be elusive.

13 Meanwhile, over $7 billion was generated from various asset sales and other realizations. From mid-2009 until March 2011, proceeds of $3.285 billion were generated from the sale of Nortel's various business lines, including some patents. Of that amount, $2.85 billion is available for allocation. In June 2011, proceeds of approximately $4.5 billion were generated from the sale of Nortel's residual intellectual property, consisting of approximately 7,000 patents and patent applications, to the Rockstar consortium. In total, approximately $7.3 billion is currently held in escrow.

14 By orders dated January 21, 2010, the Canadian and U.S. courts approved a "Final Canadian Funding and Settlement Agreement". The Agreement addressed a number of issues and allowed NNI a $2 billion claim against NNL in NNL's *CCAA* proceeding, which claim is not subject to offset or counterclaims.

15 The parties still could not agree on an Interim Sales Protocol or on allocation. In the spring of 2013, the Canadian court and the U.S. bankruptcy court granted orders approving an "Allocation Protocol". The purpose of this Protocol was to set out "binding procedures for determining the allocation of the Sale Proceeds among the Selling Debtors" [7]. It provided for a joint hearing to determine allocation before the Canadian court and the U.S. bankruptcy court. [8] Any party in interest was at liberty to advance any theory on allocation. Leave to appeal that order was denied by this court on June 20, 2013.

16 The issue of allocation of the Lockbox Funds then proceeded to trial.

C. Trial Judge's Decision

(1) Trial Decision

17 The trial judge's reasons may be summarized. He commenced by reviewing the history of the Nortel Group. He described the operations and the four main product groups or lines of business. Before turning to his analysis of the legal issues, he made a number of important findings about the Nortel Group's structure. He found, and repeatedly reiterated, that the Nortel Group operated as a highly-integrated multinational enterprise. For instance, he stated:

> [16] The Nortel Group operated along business lines as a highly integrated multinational enterprise with a matrix structure that transcended geographic boundaries and legal entities organized around the world. Each entity, such as NNL, NNI, NNUK, NN Ireland and NNSA, was integrated into regional and product line management structures to share information and perform research and development ("R&D"), sales and other common functions across geographic boundaries and across legal entities. The matrix structure was designed to enable Nortel to function more efficiently, drawing on employees from different functional disciplines worldwide, allowing them to work together to develop products and attract and provide service to customers, fulfilling their demands globally.
>
> [17] As a result of Nortel's matrix structure, no single Nortel entity, either NNL or any of the other Canadian debtors in Canada, NNI or any of the other US debtors in the United States or NNUK or any of the other EMEA debtors, was able to provide the full line of Nortel products and services, including R&D capabilities, on a stand-alone basis. While Nortel ensured that all corporate entities complied with local laws regarding corporate governance, no corporate entity carried on business on its own.

18 The trial judge also found that R&D, which was performed at labs around the world, was the primary driver of Nortel's value and profit.

19 After reviewing the necessary background, the trial judge turned to the legal issues before him, starting with the interpretation of the Master Research and Development Agreement ("MRDA"). The MRDA dealt with transfer-pricing arrangements, effective from 2001 onwards, among NNL, NNI, NNUK, NNSA and NN Ireland, who were parties to the agreement. [9]

20 The parties took differing and competing positions on the meaning and application of the MRDA:

- The Monitor (on behalf of the Canadian Debtors), supported by the Canadian Creditors' Committee ("CCC"), took the position that under the MRDA, NNL owned the IP whereas other participants to the MRDA were simply licensees. They argued that the proceeds derived from the sale of the residual IP belonged exclusively to NNL.

- The U.S. Debtors and other U.S. interests, including the Bondholders, argued that NNI and the other licensees held all of the rights and value in the IP in their respective exclusive territories as defined in the MRDA.

- The EMEA Debtors asserted that parties to the MRDA jointly owned all of the IP in proportion to their financial contributions to R&D and that all should share in the sale proceeds attributable to IP in those same proportions. The joint ownership arose independent of, but was recognized in, the MRDA.

- The UKPC took the position that the MRDA should not govern allocation and that a *pro rata* allocation based on a *pari passu* distribution should be used. The CCC also adopted this as its alternative position.

21 The trial judge found that, by its terms, the MRDA was to be construed in accordance with, and governed by, Ontario law. He reviewed the applicable principles of contractual interpretation, including the law on factual matrix (surrounding circumstances), commercial reasonableness, and recitals. In reviewing the law, he considered the recent authority from the Supreme Court of Canada on contractual interpretation, *Creston Moly Corp. v. Sattva Capital Corp.*, 2014 SCC 53, [2014] 2 S.C.R. 633 (S.C.C.), which was released during the course of the trial. He considered in detail the parties' positions, the language of the MRDA and evidence on factual matrix.

22 He concluded that the MRDA was an operating agreement and was not intended to, nor did it, deal with the disposal of all of Nortel's assets in a situation in which no revenue was being earned and no profits or losses were occurring. Rather, he found that the MRDA was developed for, and driven by, transfer-pricing concepts for tax purposes and did not govern allocation after Nortel ceased operations:

> [177] I accept that the MRDA was a transfer pricing document created for tax purposes. The licenses were a part of it. The licenses granted under it were never dealt with separately from the MRDA. Their only purpose was to support the intended tax treatment resulting from the MRDA.
>
> .....
>
> [185] I conclude that the circumstances surrounding the creation of the MRDA lead to no other result but that the construct of legal title to the NN Technology being in NNL in return for NNL granting exclusive licenses to the Licensed Participants was only for the purpose of supporting the proposed method to split profits or losses on a tax efficient basis while Nortel operated as a going concern business. The agreement in its application was intended to apply only to Nortel while it operated and not to deal with rights after Nortel and its subsidiaries stopped operating its businesses.

23 Thus, he rejected the primary positions of the Monitor, the CCC, the U.S. Debtors and other U.S. interests, as well as the EMEA Debtors' joint ownership theory.

24 Having found that the MRDA did not govern allocation on Nortel's insolvency and having rejected the joint ownership theory, the trial judge turned to the metric to be used to allocate the Lockbox Funds. He found that the intangible assets that were sold were not separately located or owned in any one jurisdiction. Rather, they were created by all of the so-called "Residual Profit Entities" or "RPEs" (namely, NNL, NNI, NNUK, NNSA and NN Ireland), which were located in different jurisdictions. In addition, the matrix structure allowed Nortel to draw on employees from different functional disciplines worldwide, regardless of region or country, according to need.

25 He held that NNL was not entitled to the proceeds of sale simply because the patents were in its name:

> [197] This was not one corporation and one set of employees inventing IP that led to patents. Nortel was a highly integrated multi-national enterprise with all RPEs doing R&D that led to patents being granted. It was R&D that drove Nortel's business. R&D and the intellectual property created from it was the primary driver of Nortel's value and profits. All parties agree on that. It would unjustly enrich NNL to deprive all of the other RPEs of the work that they did in creating the IP just because the patents were registered in NNL's name.

26 He determined that he had wide powers under the *CCAA* to do what was just in the circumstances. Section 11 of the *CCAA*, which reflected prior jurisprudence, expressly provides that a court may make any order it considers appropriate in the circumstances, subject to the provisions of the Act. He wrote:

> [208] In this case, insolvency practitioners, academics, international bodies, and others have watched as Nortel's early success in maximizing the value of its global assets through cooperation has disintegrated into value-erosive adversarial and territorial litigation described by many as scorched earth litigation. The costs have well exceeded $1 billion. A global solution in this unprecedented situation is required and perforce, as this situation has not been faced before, it will by its nature involve innovation. Our courts have such jurisdiction. [Footnote omitted.]

27 He observed that it is a fundamental tenet of insolvency law that all debts be paid *pari passu* and that all unsecured creditors receive equal treatment. In his view, a *pro rata* allocation could be achieved by directing an allocation of the Lockbox Funds to each Debtor Estate based on the percentage that the claims against that Estate bore to the total claims against all of the Debtor Estates.

28 In reaching this conclusion, the trial judge dealt with the argument that a *pro rata* allocation would amount to substantive consolidation. He concluded that a *pro rata* allocation would not constitute substantive consolidation in

the unique circumstances of this case. In any event, even if it were substantive consolidation, there was precedent that justified substantive consolidation in this case: *Lehndorff General Partner Ltd., Re* (1993), 17 C.B.R. (3d) 24 (Ont. Gen. Div. [Commercial List]); *PSINET Ltd., Re* (2002), 33 C.B.R. (4th) 284 (Ont. Gen. Div. [Commercial List]); *Northland Properties Ltd., Re* (1988), 29 B.C.L.R. (2d) 257 (B.C. S.C.).

29 Ultimately, he concluded that the Lockbox Funds were to be allocated on a *pro rata* basis in accordance with certain governing principles, which are outlined below.

30 After his reasons were released, the U.S. Debtors supported by the Official Committee, the Ad Hoc Group of Bondholders and the Law Debenture Trust Company of New York filed motions for clarification, reconsideration or amendment in Canada and the U.S. and a number of points were clarified.

31 In the end result, the judgment that was signed, issued and entered on April 26, 2016 provided that the allocation proceed on a *pro rata* basis in accordance with the following principles:

(a) Each Debtor Estate [10] is to be allocated that percentage of the Lockbox Funds that the total allowed pre-filing claims against that Debtor Estate bear to the total allowed pre-filing claims against all Debtor Estates.

(b) In determining what the claims are against the Debtor Estates, pre-filing claims of the kind provable under the *Companies' Creditors Arrangement Act* that have received court approval and which have been paid may be taken into account to the extent that they have been paid under the settlement.

(c) In determining what the pre-filing claims are against each Debtor Estate, a claim that can be made against more than one Debtor Estate can only be calculated and recognized once.

i. Claims on bonds are to be made on the Debtor Estate of the issuer and shall be included in that Debtor Estate's total allowed claims for the purpose of determining its allocation. A claim can be recognized by the Debtor Estate that guaranteed the bond, but those claims will not be taken into account in determining the claims against the Debtor Estates for allocation purposes.

ii. If the UK Pension Claimants make a claim for the approximately £2.2 billion deficit in the NNUK pension plan against NNUK and also against other EMEA Debtors or the EMEA Non-Filed Entities, the claim against NNUK will be taken into account in determining claims against the Debtor Estates for allocation purposes but the additional claims against the EMEA Debtors or the EMEA Non-Filed Entities will not be taken into account in determining the claims against the Debtor Estates for allocation purposes.

(d) Subject to the general proviso in (c), above, in respect of claims that can be made against more than one Debtor Estate, pre-filing intercompany claims against a Debtor Estate shall be included in the determination of the claims against that Debtor Estate for purposes of its allocation.

(e) The following specific pre-filing claims shall be included in the determination of the allowed claims against NNL for purposes of determining its allocation:

i. the US$2.0627 billion claim of NNI against NNL that was approved by this Court and the U.S. Court;

ii. the claims of NNUK and Nortel Networks SpA against NNL pursuant to the Agreement Settling EMEA Canadian Claims and Related Claims dated July 9, 2014; and

iii. the claim of the UK Pension Claimants against NNL recognized in this Court's judgment of December 9, 2014, as such claim is finally determined.

(f) Cash on hand in any Debtor Estate will not be taken into account in determining its allocation. Each Debtor Estate with cash on hand will continue to hold that cash and deal with it in accordance with its administration.

D. Analysis

32 Six moving parties now seek leave to appeal from the trial judge's allocation decision: the U.S. Debtors, the Ad Hoc Group of Bondholders, the Conflicts Administrator of Nortel Networks S.A., the Official Committee of Unsecured Creditors of NNI and others, the Bank of New York Mellon as Indenture Trustee, and the Nortel Trade Claims Consortium.

33 We will commence our analysis by discussing the test for leave to appeal under the *CCAA* and then address the moving parties' positions in relation to that test.

(1) Test for Leave to Appeal

34 Section 13 of the *CCAA* provides that any person dissatisfied with an order or a decision made under the Act may appeal from the order or decision with leave. Leave to appeal is granted sparingly in *CCAA* proceedings and only where there are serious and arguable grounds that are of real and significant interest to the parties. In addressing whether leave should be granted, the court will consider whether:

(a) the proposed appeal is *prima facie* meritorious or frivolous;

(b) the points on the proposed appeal are of significance to the practice;

(c) the points on the proposed appeal are of significance to the action; and

(d) whether the proposed appeal will unduly hinder the progress of the action.

See, for e.g.: *Stelco Inc., Re* (2005), 75 O.R. (3d) 5 (Ont. C.A.), at para. 24; *Timminco Ltd., Re*, 2012 ONCA 552, 2 C.B.R. (6th) 332 (Ont. C.A.), at para. 2; and *Nortel Networks Corp., Re*, 2013 ONCA 427, 5 C.B.R. (6th) 254 (Ont. C.A.), at para. 3.

(a) Whether Appeal is Prima Facie Meritorious

35 The moving parties take the position that leave should be granted because the appeal is *prima facie* meritorious. In making that argument, they raise three main issues — substantive consolidation, the interpretation of the MRDA, and questions of fairness. We will deal with each issue in turn.

(i) Substantive consolidation

Position of the Moving Parties

36 First, the moving parties submit that the trial judge erred in not recognizing that the allocation ordered departed from "corporate separateness" and was a form of substantive consolidation.

37 Secondly, it is alleged that the trial judge erred by applying an inappropriately low threshold for the application of substantive consolidation.

38 In its supplementary factum, the Bank of New York Mellon, as Indenture Trustee, makes a related argument. It submits that since the Nortel proceeding no longer involves a restructuring, the *CCAA*'s purpose is spent and the proceeds should thereafter be distributed under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*"), or at least in a manner consistent with the *BIA* scheme. It says the *BIA* does not contemplate consolidation but rather distribution on an entity-by-entity basis.

• There is "no recognized measurable right in any one of the selling Debtor Estates to all or a fixed portion of the proceeds of sale": para 224.

• "Nortel has had significant difficulty in determining the ownership of its princip[al] assets, namely the $7.3 billion representing the proceeds of the sales of the lines of business and the residual patent portfolio", which "constitutes more than 80 per cent of the total assets of all Nortel entities": para. 222.

44 In addition to his factual findings supporting the *pro rata* order, the trial judge explained why the allocation in this case did not constitute substantive consolidation, either actual or deemed:

• The Lockbox Funds were largely due to the sale of IP and no one Debtor Estate had any right to the funds. They did not belong in whole or in part to any one Estate or combination of Estates.

• The various entities and the various Estates were not being treated as one entity and the creditors of each entity would not become creditors of a single entity. Each entity remained separate and with its own creditors.

• Each entity would maintain its own cash on hand and would be administered separately.

• The inter-company claims would not be eliminated.

45 Similarly, Judge Gross explained at p. 554 of his reasons that the *pro rata* allocation, which was not a distribution, "both recognizes the integrity of the corporate separateness and the integrated synergistic operations of Nortel." Furthermore, he noted that a "pro rata allocation does not merge the Nortel Debtors into a single survivor and does not erase intercompany claims": p. 554.

46 In our view, there is no *prima facie* merit to the argument that we should interfere with the trial judge's conclusion that the allocation decision did not amount to substantive consolidation. His conclusion was based on the nature and effect of his allocation decision and his factual findings. He made the findings having heard from 36 witnesses and having received and reviewed thousands of exhibits and dozens of deposition transcripts over the course of a six-week trial. Those factual findings were central to the result. Absent palpable and overriding error, those factual findings are afforded deference by this court: *Housen v. Nikolaisen*, 2002 SCC 33, [2002] 2 S.C.R. 235 (S.C.C.), at para. 10.

47 The moving parties also allege that the trial judge erred by applying an inappropriately low threshold for the application of substantive consolidation in finding that, even if the allocation did constitute substantive consolidation, it was permissible. They point to *Northland* as the leading authority on substantive consolidation but say that it is time to revisit that decision in Canada.

48 The trial judge correctly observed that while the *CCAA* does not expressly address the issue of substantive consolidation, jurisprudence in Canada has recognized substantive consolidation as being appropriate in certain exceptional circumstances: see, for e.g., *Lehndorff General Partner Ltd.*, *PSINet Ltd.*, and *Northland Properties Ltd.*

49 He also correctly observed that the court has jurisdiction to make any order that it considers appropriate in the circumstances under s. 11 of the *CCAA*. Although that section came into effect after the Nortel filing under the *CCAA*, it reflects past jurisprudence: *Ted Leroy Trucking Ltd., Re*, 2010 SCC 60, [2010] 3 S.C.R. 379 (S.C.C.), at para. 68. Specifically, s. 11 states:

> 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.

issues of limited application, this supports treating contractual interpretation as a question of mixed fact and law": para. 52.

- "[I]t may be possible to identify an extricable question of law from within what was initially characterized as a question of mixed fact and law .... Legal errors made in the course of contractual interpretation include 'the application of an incorrect principle, the failure to consider a required element of a legal test, or the failure to consider a relevant factor'": para. 53.

- "However, courts should be cautious in identifying extricable questions of law in disputes over contractual interpretation": para. 54.

- "The close relationship between the selection and application of principles of contractual interpretation and the construction ultimately given to the instrument means that the circumstances in which a question of law can be extricated from the interpretation process will be rare": para. 55.

58 Justice Rothstein also discussed the need to consider the surrounding circumstances, or factual matrix of a contract, when interpreting a written agreement. The goal of contractual interpretation is to ascertain the objective intentions of the parties. In doing so, "a decision-maker must read the contract as a whole, giving the words used their ordinary and grammatical meaning, consistent with the surrounding circumstances known to the parties at the time of formation of the contract": para. 47. Recognizing that words do not have an immutable meaning, the court should consider the contract's commercial purpose, taking into account its genesis, background, context, and the market in which the parties are operating.

59 In this case, the moving parties suggest that the trial judge erred in his interpretation of the MRDA and failed to pay heed to *Sattva Capital Corp.* In our view, the moving parties' arguments are not *prima facie* meritorious.

60 We are not persuaded that there is any reason to interfere with the trial judge's interpretation of the agreement on the basis of palpable and overriding error. Nor, in our view, have the moving parties pointed to any extricable legal error warranting intervention by this court.

61 As mentioned, although *Sattva Capital Corp.* was released during the course of the allocation trial, the trial judge nonetheless considered and applied *Sattva Capital Corp.* in interpreting the MRDA. In over 40 paragraphs, he addressed the relevant law on, and evidence of, factual matrix: see paras. 55 - 57, 117 - 157. He properly rejected evidence of subjective intention as being inadmissible.

62 We would also observe that, as noted by the Monitor and the Canadian Debtors, to be fully successful on their appeal, the U.S. Debtors would have to persuade the court that the trial judge should have: (i) concluded that the MRDA controlled allocation of Nortel's assets in the event of insolvency; (ii) adopted the interpretation of the MRDA advanced by the U.S. Debtors; and (iii) accepted the expert valuation evidence tendered by the U.S. Debtors.

63 The trial judge did none of these things. All of his conclusions to the contrary engage questions of fact or mixed fact and law that are well within his province.

64 For instance, the trial judge rejected the U.S. Debtors' valuation evidence as unreliable and the moving parties' factums are silent on how this finding could be overcome. The acceptance or rejection of the evidence of a witness is squarely within the fact-finding arena of the trial judge. The moving parties have suggested no reason why the trial judge's findings on valuation would be reversed.

65 In conclusion, this ground of appeal does not warrant granting leave to appeal.

(iii) Fairness to the Parties and Related Arguments

Position of Moving Parties

66 Next, the moving parties submit that they were denied procedural fairness in various respects and that the allocation decision is, among other things, arbitrary, and inequitable. In this regard, we do not propose to address every argument in the multitude of factums filed. The principal submissions on fairness and related arguments that merit comment are as follows.

67 The moving parties say they were given no notice or opportunity to make submissions on the remedy granted. Moreover, there was no record before the court on the full spectrum of claims asserted against the Selling Debtors and no one proposed the specific remedy granted.

68 The U.S. Debtors also submit that the remedy did not respond to the question before the court, which they say was the allocation of the Sale Proceeds (i.e. the proceeds from a particular Sale Transaction) among the Selling Debtors (i.e. the Nortel parties to a particular Sale Transaction). In their view, the trial judge did not answer that question but instead allocated the Sale Proceeds to Nortel entities that did not transfer assets in a particular Sale Transaction and were, thus, not entitled to any Sale Proceeds.

69 The Ad Hoc Group of Bondholders similarly submits that the trial judge answered the wrong question. For instance, it says that the only question properly before the court was to determine the relative value of the assets, rights and interests that each Selling Debtor sold or relinquished, which generated the Sale Proceeds. Moreover, they say that the decision disregards their legitimate expectations.

70 The U.S. Debtors further submit that the allocation is arbitrary since there is no logical connection between what will be or will not be counted for allocation purposes. In particular, they point to the fact the allocation excludes $4 billion in bondholder guarantee claims from the U.S. Debtors' allocation. They say that, as a result, the U.S. Debtors will receive no allocation of funds on account of approximately two-thirds of their claims.

71 Similarly, the Ad Hoc Group of Bondholders submits the allocation is arbitrary as it produces a redistribution of assets among debtors that violates the rule that equity holders get paid after creditors.

72 The Conflicts Administrator of NNSA also takes issue with the fairness of the allocation decision. It says that NNSA is prejudiced by the decision because of the relatively small quantum of its creditors' claims in comparison with those of other debtor estates.

73 Finally, the Official Committee, which represents all general unsecured creditors of the U.S. Debtors, complains that the trial judge exercised his discretion in an unprincipled way and strayed into improper "commercial judicial moralism".

Analysis

74 We are not satisfied that there is *prima facie* merit to the moving parties' submissions.

75 As explained, the trial judge was required to "determine the allocation of the Sale Proceeds among the Selling Debtors" under the Allocation Protocol.

76 Given the trial judge's conclusion that the MRDA did not govern allocation and his rejection of the EMEA Debtors' joint ownership theory, the trial judge had to determine what other metric should be used to allocate the Lockbox Funds among the U.S., Canadian and EMEA Debtor Estates.

77 The Allocation Protocol permitted submissions on "any theory of allocation". At trial, the UKPC and the CCC, in the alternative, sought a *pro rata* distribution of the funds held in escrow and each submitted expert reports that supported a *pro rata* result. Moreover, the U.S. Debtors, the Official Committee and the Ad Hoc Group of Bondholders all made submissions before the trial judge opposing a *pro rata* allocation and had an opportunity to test the evidence. They submitted a motion to strike the *pro rata* allocation evidence, attacked the reliability of the expert reports and cross-examined the experts.

78 Thus, all parties knew that a *pro rata* allocation was in play. The fact that the specifics of the allocation ordered by the trial judge were not identical to those advanced by any of the parties does not, in our view, create unfairness to the parties. This is not a situation where the trial judge addressed an issue that was not before him, failed to grapple with the arguments or evidence, or came up with a new theory of the case.

79 The two judges were not required to determine value but allocation. The IFSA provided for a right to receive an allocation of the Sale Proceeds without restricting the basis upon which that allocation might be determined by the two courts. In particular, we note that the trial judges were given authority to decide the issue of allocation. In addition to the terms of the Allocation Protocol, we note s.10(a) of the IFSA:

> [T]his Agreement is not, and shall not be deemed to be, an acknowledgement by any Party of the assumption, ratification, adoption or rejection of the Transfer Pricing Agreements or any other Transfer Pricing methodology employed by the Nortel Group or its individual members for any purpose nor shall it be determinative of, or have any impact whatsoever on, the allocation of proceeds to any Debtor from any sale of assets of the Nortel Group;
>
> [Emphasis added.]

80 We also observe that the trial judge turned his mind to expectations and found that there was no evidence to support the Bondholders' argument that their legitimate expectations would be disregarded by a *pro rata* allocation.

81 Furthermore, we see no basis for the assertion that the allocation framework is arbitrary and unfair since it excludes $4 billion in Bondholder guarantee claims from the U.S. Debtors' allocation. Under the allocation decision, a claim that can be made against more than one Debtor Estate can only be calculated and recognized once for allocation purposes. This principle is applicable to all claims. The allocation decision also specifies that claims on bonds are to be made on the Debtor Estate of the issuer. Claims on those bonds may also be made on the Debtor Estate of the guarantor but those claims will not be taken into account in determining the claims against the Debtor Estates for allocation purposes.

82 On the reconsideration motion, it was argued that the trial judge's decision should be changed to provide that the claims by the bondholders on the guaranteed bonds against the issuer and guarantor Debtor Estates should be included in the claims for allocation purposes. It was contended that, without such a change, there would be a manifest injustice, especially to the creditors of the U.S. Debtors other than the bondholders.

83 The trial judge rejected that argument, noting that the $2 billion admitted claim against NNL endures. Further, cash on hand in the U.S. Debtors' Estates would be available to their creditors. He also noted that the issue of the treatment of the guaranteed bonds, and whether they should be counted once or twice in a *pro rata* allocation, was a live issue in evidence at trial, which was open to the U.S. Debtors to explore. He found, at para. 16, that "any lack of briefing by the U.S. Debtors and the [Official Committee] was a deliberate tactic taken by them in attacking the pro rata allocation method proposed at trial". He concluded that, even if he were to reconsider the double-counting issue, he would not change his mind:

> I see no injustice in the result.... There must also be considered other claims that could be made against more than one Debtor Estate, including the pension claim by the UKPC against NNUK that could be made against other EMEA Debtors and claims that could be made on bonds issued by NNL and guaranteed by NNC. The allocation decision precludes the double counting of any such claims for allocation purposes. The U.S. Debtors and [Official Committee] do not suggest that any of these other claims should be permitted to be claimed twice for allocation purposes. I see no basis to treat the guaranteed bonds any differently for allocation purposes. The principles that govern allocation should be applied consistently to each debtor.

84 We are not persuaded that there is *prima facie* merit to the argument that the allocation is arbitrary. The trial judge was clearly alive to the fairness concerns and gave reasons for adopting the approach he did after careful consideration of the evidence and argument at trial.

85 We would also observe that there was no other clear answer to the question of who was entitled to receive the sale proceeds. As Judge Gross noted at p. 500 of his reasons, the parties "submitted widely varying approaches for deciding the issue leaving virtually no middle ground." The U.S. Debtors and Bondholders argued that in excess of $5 billion belonged to the U.S. Estate and that the Canadian Estate should receive only $0.77 billion. The Canadian Debtors and the Monitor, in sharp contrast, argued that in excess of $6 billion belonged to the Canadian Estate and that the U.S. Estate should receive just over $1 billion. The highly integrated nature of the Nortel business operations and the nature of the assets sold defied either outcome.

86 Judge Gross's comments in his reasons on the allocation trial, at pp. 532-533, accurately sum up the context in which the two courts came to adopt the *pro rata* allocation approach:

> The Court is convinced that where, as here, operating entities in an integrated, multi-national enterprise developed assets in common and there is nothing in the law or facts giving any of those entities certain and calculable claims to the proceeds from the liquidation of those assets in an enterprise-wide insolvency, adopting a prorata allocation approach, which recognizes inter-company and settlement related claims and cash in hand, yields the most acceptable result.
>
> There is nothing in the law or facts of this case which weighs in favour of adopting one of the wide ranging approaches of the Debtors. There is no uniform code or international treaty or binding agreement which governs how Nortel is to allocate the Sales Proceeds between the various insolvency estates or subsidiaries spread across the globe.

87 Nor are we satisfied that there is *prima facie* merit to the Official Committee's argument that the trial judge exercised his discretion in an unprincipled way by straying into improper "commercial judicial moralism". To the extent the Official Committee is suggesting that it amounts to judicial moralism when a judge takes into account fairness concerns, we reject that argument. The trial judge considered the evidence before him in considerable detail and worked with the facts presented to him. Based on those facts, he concluded that a *pro rata* order constituted the answer to the allocation issue. The fact that the answer is also fair should not detract from the force of his conclusion.

88 Finally, we are not persuaded that there is any merit to the argument that the allocation violates the rule that equity holders get paid after creditors. The Ad Hoc Group of Bondholders submits that the trial judge's decision results in NNL (NNI's parent company) receiving allocation proceeds from the sale of NNI's assets and rights that ought to have been allocated to the NNI estate for the benefit of NNI's creditors. This argument is premised on NNI having a right to the particular proceeds as a result of the MRDA interpretation advanced by the U.S. Debtors and Bondholders. As we have discussed above, the trial judge rejected that argument.

89 For these reasons, we conclude that none of the fairness and related arguments put forward by the moving parties are *prima facie* meritorious.

(b) Significance of Issues to the Practice

Position of Moving Parties

90 The moving parties submit that the trial judge's decision presents important issues of first impression in the cross-border insolvency context. They submit that, without appellate intervention, there is a risk substantive consolidation will become far more widely available. In addition, they say that it creates significant uncertainty on the separation of subsidiaries within a corporate group and on the consequences of an insolvency proceeding on the rights of stakeholders, including creditors. In their submission, an appeal would permit this court to clarify these issues. Furthermore, the appeal would allow this court to clarify the proper interpretation and effect of *Sattva Capital Corp.* on commercial agreements.

Analysis

91 As discussed above, the moving parties have raised three main issues they say warrant leave — namely, substantive consolidation, the interpretation of the MRDA, and fairness. Of the three issues, the moving parties submit that the first two raise issues of significant interest to the practice.

92 We disagree.

93 The facts of this case are unique and exceptional. As we have already discussed, substantive consolidation is not engaged and so this case would not provide an opportunity for this court to provide guidance on that question. Nor does this case engage any issues that require any clarification on the application of *Sattva Capital Corp.* . In short, granting leave would not provide an opportunity for this court to provide guidance on legal issues of significance to the practice.

(c) Significance of Issues to the Action

Position of Moving Parties

94 The moving parties state that the allocation of the Lockbox Funds is the overriding issue in the *CCAA* proceedings.

Analysis

95 We accept that the allocation of the Lockbox Funds is a significant issue in this *CCAA* proceeding. That said, we are of the view that, standing alone, this factor is insufficient to warrant granting leave to appeal. To perhaps state the obvious, typically parties tend to seek leave to appeal a decision that is of significance to an action.

(d) Progress of Proceedings

Position of Moving Parties

96 The moving parties submit that the proposed appeal will not unduly hinder the progress of Nortel's *CCAA* proceeding. They state that many steps and issues remain before creditor distributions can be made, including the determination of claims. In addition, the allocation decisions of the Canadian court and the U.S. court must both be final orders in their respective jurisdictions before funds can be released from escrow. It is argued that this court should grant leave to ensure that it maintains the ability to address any issues should Judge Gross's decision be varied or overturned on appeal.

97 The moving parties also make the point that there are no operating businesses that are in the process of restructuring because the Nortel businesses and assets have been liquidated and the joint trial was a "stand-alone component" of the *CCAA* proceeding. Thus, it is argued that the traditional concerns leading courts to "sparingly" grant leave to appeal in *CCAA* proceedings are not applicable here. In fact, the Official Committee submits that where an appeal would have existed as of right under the *BIA*, it is nonsensical to deny leave here simply because Nortel's liquidation proceeded under the *CCAA*.

Analysis

98 This brings us to the final consideration: progress. Repeatedly, the parties have been encouraged to resolve their differences, but without success. For instance, in a 2011 decision, *Nortel Networks Inc., Re*, 669 F.3d 128 (U.S. C.A. 3rd Cir. 2011), the Third Circuit Court of Appeals admonished the parties at p. 143:

> We are concerned that the attorneys representing the respective sparring parties may be focusing on some of the technical differences governing bankruptcy in the various jurisdictions without considering that there are real live individuals who will ultimately be affected by the decisions being made in the courtrooms. It appears that the largest claimants are pension funds in the U.K. and the United States, representing pensioners who are undoubtedly

> dependent, or who will become dependent, on their pensions. They are the Pawns in the moves being made by the Knights and the Rooks.
>
> Mediation, or continuation of whatever mediation is ongoing, by the parties in good faith is needed to resolve the differences. [Footnote omitted.]

99 Former Chief Justice Winkler also encouraged the parties to find a way to resolve this matter. In April 2012, he warned about the "prospect of additional delays and the potential for conflicting decisions" if the parties failed to reach a negotiated settlement.

100 Numerous mediations have been ordered but have failed.

101 In the Annual Review of Insolvency, Kevin P. McElcheran described *Nortel* as a case that has become "an emblem of waste and dysfunction in a system intended to foster consensus based solutions to commercial insolvency", noting that it has "eclipsed all previous Canadian cases in both duration and expense": 2014 Ann. Rev. Insolv. L. 24 at p. 24. And that was in 2014.

102 Consistent allocation decisions have been issued by the Canadian and U.S. courts. A further appeal proceeding in Canada would achieve nothing but more delay, greater expense, and an erosion of creditor recoveries. There are asymmetric appeal routes in Canada and the U.S. However, we do not accept that the separate appeal proceedings in the U.S. somehow diminish the need to bring these proceedings in Canada to a conclusion. In our view, any additional step is a barrier to progress.

103 Furthermore, the fact that this case is a liquidation and not a restructuring does not render delay immaterial, where so many individuals and businesses continue to await a resolution of this proceeding. The potential of an interim distribution, remote or otherwise, does not alter this reality. In addition, the parties acceded to a liquidation under the *CCAA*. They cannot now reject the parameters of that statute, which requires leave to appeal, and where the jurisprudence on the applicable test is settled and long-standing.

E. Standing Issue

104 There is the additional issue of the standing of the Nortel Trade Claims Consortium that needs to be addressed. It represents a group of creditors that collectively holds over $130 million in unsecured claims against NNI and certain of its U.S. affiliates. It includes institutional investors and former Nortel employees. Unlike other U.S. creditors, the Consortium's sole recourse is against the U.S. Debtors' estates.

105 At trial, the Consortium was represented by the Official Committee. It says that, given the trial decision, its interests may diverge from those of the rest of the Official Committee. It submits that the Consortium should have standing to seek leave to appeal. It relies on the court's jurisdiction to grant leave to appeal, pursuant to s. 13 of the *CCAA*, to "any person dissatisfied with an order or a decision made under [the] Act". It argues that the trial judge exceeded his jurisdiction by deciding matters that are properly for the U.S. court to decide.

106 It is unnecessary to decide the standing issue. Even if the Consortium had standing, we would dismiss its leave motion for the same reasons we have dismissed the other leave motions. In any event, we see no merit in its argument that the trial judge exceeded his jurisdiction.

F. Disposition

107 In conclusion, we are not persuaded that the test for leave to appeal has been met. For these reasons, we dismiss all of the motions for leave to appeal.

Motions dismissed.

Footnotes

1 All references to dollars are to U.S. dollars, unless otherwise specified.

2 Judge Gross's reasons are reported at 532 B.R. 494 (U.S. Bankr. D. Del. 2015).

3 In accordance with the directions of the Court of Appeal case management judge, there was one main factum filed on behalf of the moving parties by the U.S. Debtors and one main factum filed on behalf of the responding parties by the UKPC. Six supplementary factums and one reply factum were also filed.

4 With the exception of Nortel Networks (CALA) Inc.

5 The Joint Administrators were also party to the IFSA but only for the purposes of Section 17 (No Personal Liability of the Joint Administrators).

6 A description of "Selling Debtor" is found in s.12 (a) of the IFSA: "Each Debtor hereby agrees that its execution of definitive documentation with a purchaser (or, in the case of any auction, the successful bidder in any such auction) of, or closing of any sale of, material assets of any of the Debtors to which such Debtor (a "Selling Debtor") is proposed to be a party..."

7 Selling Debtors was defined in the Allocation Protocol as the "Canadian Debtors, U.S. Debtors, EMEA Debtors and Nortel Networks Optical Components Ltd., Nortel Networks AS, Nortel Networks AG, Nortel Networks South Africa (Pty) Limited, and Nortel Networks (Northern Ireland) Limited."

8 The EMEA Debtors were held to have attorned to the jurisdiction of the Canadian court and the U.S. bankruptcy court.

9 Nortel Networks Australia was also a party to the agreement. It ceased being a Residual Profit Entity on December 31, 2007.

10 The order defines "Debtor Estate" as "each of the individual legal entities" set out in Schedule B. Schedule B lists the 45 entities, including the Canadian Debtors, the U.S. Debtors, the EMEA Debtors and five "EMEA Non-Filed Entities" who have not commenced insolvency proceedings. See also the similar definition given to Selling Debtors under the Allocation Protocol.

End of Document

Tab 4

2017 ONSC 5572
Ontario Superior Court of Justice [Commercial List]

Mercado Capital Corporation v. Qureshi

2017 CarswellOnt 15109, 2017 ONSC 5572, 284 A.C.W.S. (3d) 254

MERCADO CAPITAL CORPORATION (Applicant) and HAFSA FAISAL QURESHI and POLLARD & ASSOCIATES INC., Trustee in Bankruptcy for the Estate of Faisal Iqbal Qureshi (Respondents)

Hainey J.

Heard: July 7, 2017
Judgment: September 20, 2017
Docket: CV-16-11610-00CL

Counsel: Michael S. Myers, James S. Quigley, for Applicant
Veena Pohani, Kristine Holder, for Respondent, Hafsa Faisal Qureshi

Subject: Estates and Trusts; Family; Insolvency; Property

APPLICATION by creditor for declaration that what it characterized as notional gift of 50 per cent of equity in matrimonial home to wife was void as undervalue transfer.

Hainey J.:

Background

1 The applicant, Mercado Capital Corporation, seeks a declaration that what it characterizes as a notional gift of 50% of the equity in property located at 55 Davina Circle, Aurora, ("Davina") by Faisal Iqbal Qureshi ("Faisal"), a bankrupt, to his spouse, Hafsa Faisal Qureshi ("Hafsa"), is a transfer at undervalue and is therefore void pursuant to s. 96(1)(b)(i) of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("*BIA*").

2 Faisal and Hafsa were married for 15 years. They have three children. Their eldest child has been diagnosed with autism and epilepsy. He is a special needs child who requires around-the-clock care.

3 Hafsa was a stay at home mother throughout most of the marriage. She cared for their children and did all of the domestic work and household management. She supported Faisal at home while he earned the family income by operating various businesses.

4 In 2011, Faisal and Hafsa bought a family home at 278 Selwyn Avenue in Richmond Hill ("Selwyn"). According to Hafsa, her parents contributed $50,000 toward the purchase price of the home. Faisal and Hafsa lived there with their children for around four years. Selwyn was registered in Faisal's name although both Faisal and Hafsa believed that they each owned an equal share.

5 On February 18, 2015, Hafsa entered into an Agreement of Purchase and Sale on behalf of Faisal and herself to purchase Davina.

6 On June 30, 2015, Faisal and Hafsa sold Selwyn. The net proceeds from the sale were $372,177. They then closed the purchase of Davina on the same date. The purchase of Davina was funded with the $372,177 net proceeds from the sale of Selwyn, $256,240 from funds obtained by Faisal, $89,654 from Hafsa's parents and mortgage funds of $1,902,081.

Faisal and Hafsa were registered on title as joint tenants. They believed that they each had a 50% interest in Davina because it was their matrimonial home.

7 In 2016, Faisal and Hafsa's marriage broke down. Faisal moved out and began a relationship with another woman. For several months he lived with this woman in Dubai while Hafsa was left on her own in Aurora with their three children.

8 On June 2, 2016, the applicant brought an application for bankruptcy against Faisal. Faisal did not oppose the application and he was adjudged bankrupt on July 5, 2016. Pollard & Associates Inc. was appointed by the court as the trustee in bankruptcy of Faisal's estate ("Trustee").

9 In the summer of 2016, Davina was sold for $2,838,000. Faisal and Hafsa realized net proceeds from the sale of approximately $696,815. Hafsa's 50% share of the net proceeds is currently being held by the Trustee pending the outcome of this application.

10 Faisal is alleged to have been involved in a multi-million dollar fraud. In February 2017, while en route from Dubai to London, England, Faisal's passport was cancelled and he was forced to return to Canada. He was arrested upon arriving in Toronto and charged with multiple counts of fraud. He is currently living with his father in Markham. There is no evidence that Hafsa was aware of Faisal's alleged fraudulent activities.

11 Hafsa has no separation agreement with Faisal, no court ordered support or any firm commitment from him to pay child and spousal support. Davina was Hafsa's only asset. Because all of the proceeds from Davina are currently being held by the Trustee as a result of this application, Hafsa is entirely dependent on Faisal's goodwill and willingness to pay family support. She is currently living with her mother in Richmond Hill.

12 According to Hafsa, she needs her share of the net proceeds from Davina in order to build an independent life with her three children.

Facts

13 The parties entered into an agreed statement of facts that is attached as Appendix 1. It contains all of the relevant facts necessary for the determination of this motion.

Issue

14 The issue that I must determine is whether Hafsa is entitled to 50% of the net proceeds from the sale of Davina or whether she is disentitled to receive this amount because it constitutes a transfer from Faisal to her at undervalue and is therefore void pursuant to s. 96(1)(b)(i) of the *BIA*.

Positions of the Parties

15 The applicant submits that because Faisal was the sole wage earner in the family and Hafsa was a "stay at home" mother earning no income, Faisal "notionally" gifted one-half of the purchase price of Davina to her in order to enable her to acquire a one-half interest in their new home.

16 The applicant further submits that Faisal's "gift" to Hafsa had a fair market value of $359,035 and that Hafsa did not provide Faisal with any consideration for this gift. Accordingly, the gift to Hafsa, which occurred on June 30, 2015, less than one year before Faisal's initial bankruptcy event on June 2, 2016, is a transfer at undervalue pursuant to s. 96(1)(b)(i) of the *BIA*. It is therefore void as against the applicant.

17 Hafsa submits that there was no transfer or gift from Faisal to her when they purchased Davina and took title as joint tenants. She submits that even if there was, Hafsa's domestic services and childcare and her parents' direct financial contribution toward the purchase price of Selwyn and Davina constitute sufficient consideration to support the transfer to her of one-half of the equity in Davina, which was their matrimonial home.

Analysis

18 Section 96(1)(b) of the *BIA* provides as follows:

Transfer at undervalue

96. (1) On application by the trustee, a court may declare that a transfer at undervalue is void as against, or, in Quebec, may not be set up against, the trustee — or order that a party to the transfer or any other person who is privy to the transfer, or all of those persons, pay to the estate the difference between the value of the consideration received by the debtor and the value of the consideration given by the debtor — if

. . .

(b) the party was not dealing at arm's length with the debtor and

(i) the transfer occurred during the period that begins on the day that is one year before the date of the initial bankruptcy event and ends on the date of the bankruptcy; or

(ii) the transfer occurred during the period that begins on the day that is five years before the date of the initial bankruptcy event and ends on the day before the day on which the period referred to in subparagraph (i) begins and

(A) the debtor was insolvent at the time of the transfer or was rendered insolvent by it, or

(B) the debtor intended to defraud, defeat or delay a creditor.

19 The applicant submits in its factum that "this application fits squarely within the confines of the ratio" of the decision of Myers J. in *Lee, Re*, 2017 ONSC 388 (Ont. S.C.J.) at para. 16 as follows:

Section 96 imposes a strict test to remedy non-arm's length transfers among family members. While the statute allows relief using the word "may", in my view, on proof of the requisite facts, relief should be granted at the amount calculated in accordance with the statute, in all but the most exceptional circumstances. This is especially so in the case of a non-arm's length transaction that is attacked within one year... In my view, judgment should be nearly automatic in such case.

20 I disagree that the decision in *Re Lee* applies to this case. There is much to distinguish this case from the case of *Re Lee* . In *Re Lee* , the bankrupt and his spouse were joint tenants of the property in question and severed their joint tenancy by the bankrupt transferring his one-half interest in the property to his spouse for nominal consideration. This left the bankrupt with no interest on title to the property within one year of the initial bankruptcy event. In my view this clearly constituted a deliberate attempt by the bankrupt to defeat his creditors. In this case there is no evidentiary basis for concluding that Faisal was attempting to defeat his creditors when Davina was purchased and held by Hafsa and him as joint tenants. This is a significant difference from the facts in *Re Lee* .

21 I agree with Myers J.'s conclusion in *Re Lee* on the facts of that case. However, I have concluded that his decision does not apply in this case because of the significant differences in the underlying facts.

22 In *Re Lee* , Myers J. acknowledged the discretionary nature of the relief provided for under s. 96 which provides that the court "may" declare a transfer at undervalue void. There is no jurisprudence concerning when it is appropriate to exercise the court's discretion not to declare a transfer at undervalue void under s. 96 of the *BIA*. It is, therefore, helpful to review the jurisprudence that considered the section of the *BIA* that s. 96 replaced when amendments were made to the *BIA* in 2009.

23 Section 96 of the *BIA* replaced the reviewable transaction provision contained in the former s. 100 of the *BIA*. This previous section also gave the court discretion by providing that a court "may" give judgment to the trustee for the difference in the value of the consideration in a reviewable transaction.

24 The relevant provisions of the previous s. 100 provided as follows:

> **Examination of consideration in a reviewable transaction**
>
> **100 (1)** Where a bankrupt sold, purchased, leased, hired, supplied or received property or services in a reviewable transaction within the period beginning on the day that is one year before the date of the initial bankruptcy event and ending on the date of the bankruptcy, both dates included, the court may, on the application of the trustee, inquire into whether the bankrupt gave or received, as the case may be, fair market value in consideration for the property or services concerned in the transaction.
>
> **Judgment for difference**
>
> **(2)** Where the court in proceedings under this section finds that the consideration given or received by the bankrupt in the reviewable transaction was conspicuously greater or less than the fair market value of the property or services concerned in the transaction, the court <u>may</u> give judgment to the trustee against the other party to the transaction, against any other person being privy to the transaction with the bankrupt or against all those persons for the difference between the actual consideration given or received by the bankrupt and the fair market value, as determined by the court, of the property or services concerned in the transaction.
>
> (Emphasis added)

25 The Ontario Court of Appeal in *Standard Trustco Ltd. (Trustee of) v. Standard Trust Co.* (1995), 26 O.R. (3d) 1 (Ont. C.A.) held that granting the remedy under the former s. 100 (2) of the *BIA* was discretionary having regard to factors such as the good faith of the parties, the intention with which the transaction took place and whether fair value was given and received by the parties.

26 The Supreme Court of Canada in *People's Department Stores Ltd. (1992) Inc., Re*, 2004 SCC 68 (S.C.C.), endorsed the view of the Ontario Court of Appeal in *Standard Trust Co* . and held that "equitable principles guide the exercise of discretion".

27 Major and Deschamps JJ. concluded as follows at paras. 81 and 82 of the Supreme Court's decision in *Peoples Department Stores* :

> 81. The word "may" is found in both ss. 100(1) and 100(2) of the BIA with respect to the jurisdiction of the court. In *Standard Trustco Ltd. (Trustee of) v. Standard Trust Co.* (1995), 26 O.R. (3d) 1 (Ont. C.A.), a majority of the Ontario Court of Appeal held that, even if the necessary preconditions are present, the exercise of jurisdiction under s. 100(1) to inquire into the transaction, and under s. 100(2) to grant judgment, is discretionary. Equitable principles guide the exercise of discretion. We agree.
>
> 82. Referring to s. 100(2) of the BIA, in *Standard Trustco, supra*, at p. 23, Weiler J.A. explained that:
>
>> When a contextual approach is adopted it is apparent that although the conditions of the section have been satisfied the court is not obliged to grant judgment. The court has a residual discretion to exercise. The contextual approach indicates that the good faith of the parties, the intention with which the transaction took place, and whether fair value was given and received in the transaction are important considerations as to whether that discretion should be exercised.
>
> We agree with Weiler J.A. and adopt her position; ...

28 In light of this jurisprudence, which I have concluded applies to the exercise of my discretion under s. 96 of the *BIA*, it is not necessary for me to decide whether Hafsa's 50% interest in the equity of Davina resulted from a transfer at undervalue contrary to s. 96(1)(b)(i) of the *BIA*. Even if it did, which I doubt, I would exercise my equitable discretion not to declare her 50% interest in Davina void.

29 I have arrived at this conclusion by taking a contextual approach to the evidence. I find that Faisal and Hafsa were acting in good faith and intended that their joint tenancy in Davina represented the fact that it was their matrimonial home in which they each believed that they held a 50% interest. I find that there was no intention on the part of Faisal to defeat his creditors by taking title to Davina as a joint tenant with Hafsa. In adopting an equitable approach to the exercise of my discretion I have relied upon the following factors in deciding not to declare Hafsa's 50% interest in Davina void:

• Faisal's and Hafsa's good faith;

• The fact that Faisal did not take joint title in Davina to defeat his creditors;

• Hafsa's substantial non-monetary contribution to the family by her hard work managing the household and caring for their children, particularly in light of their special needs child;

• Hafsa's parents' contributions to the purchase price of both of their matrimonial homes;

• Hafsa's and Faisal's honest belief that Hafsa was entitled to a 50% interest in Davina because it was their matrimonial home;

• The fact that Hafsa and her children have no other guaranteed form of financial support and that Davina was her only asset which she needs to carry on an independent life with her children; and

• The fact that the Agreement of Purchase and Sale for Davina was signed by Hafsa in February 2015, well before the one year period preceding Faisal's initial bankruptcy event.

Conclusion

30 For all of these reasons the application is dismissed.

31 The Trustee is hereby ordered to deliver to Hafsa her share of the net proceeds from the sale of Davina within 15 days.

Costs

32 Hafsa is entitled to her costs of this application. If the parties cannot agree on costs they may schedule a 9:30 a.m. attendance with me at which time I will determine the issue of costs. The parties are to provide me with their costs outlines prior to the attendance.

33 I thank counsel for their helpful submissions.

Application dismissed.

Appendix 1

Court File No. CV-16-11610-00CL

ONTARIO SUPERIOR COURT OF JUSTICE COMMERCIAL LIST

BETWEEN:

MERCADO CAPITAL CORPORATION

Applicant

-and-

HAFSA FAISAL QURESHI and POLLARD & ASSOCIATES INC., Trustee in Bankruptcy for the Estate of Faisal Iqbal Qureshi

Respondents

AGREED STATEMENT OF FACTS

The Applicant MERCADO CAPITAL CORPORATION and the Respondent HAFSA FAISAL QURESHI agree to the following facts for the purpose of the hearing of this Application:

1. The Respondent Hafsa Faisal Qureshi ("**Mrs. Qureshi**") is the spouse of Faisal Iqbal Qureshi ("**Mr. Qureshi**"). They were married on December 28, 2001, They have three children together.

2 Mr. Qureshi is the sole owner of a business corporation named Client360 Group Inc. ("Client360").

3. Mrs. Qureshi has no ownership interest in Client360.

4. Throughout their marriage, Mrs. Qureshi has never assisted Mr. Qureshi with any of his business activities.

5. Throughout their marriage, Mrs. Qureshi has not been employed outside the home. Mrs. Qureshi obtained her MBA but did not work outside the house especially after Mr. and Mrs. Qureshi's eldest child became sick with autism and epilepsy.

6. Mr. and Mrs. Qureshi resided together at Mr. Qureshi's parents' house from the date of their marriage until 2011.

7. At some point prior to July 25, 2011, Mr. Qureshi borrowed the sum of $50,000.00 from Mrs. Qureshi's parents. Mr. Qureshi offered to repay the loan prior to purchasing the Selwyn Road property (as defined in paragraph 8). Mrs. Qureshi's parents declined his offer and said he could use the money for the purchase of Selwyn Road.

8. Mr. Qureshi purchased a house municipally known as 278 Selwyn Road ("Selwyn Road") in Richmond Hill on July 25, 2011. Only Mr. Qureshi held registered title to the Selwyn Road property.

9. Mr. Qureshi and Mrs. Qureshi resided at the Selwyn Road property together as husband and wife. This was a matrimonial home.

10. Mrs. Qureshi was responsible for raising the children and the performance of all household responsibilities.

11. Mr. Qureshi mortgaged the Selwyn Road property to Bay Point Financial Services Inc. ("Bay Point") on May 28, 2014 in exchange for a loan of $250,000.00 (the "Second Mortgage") which was fully advanced pursuant to his direction.

12. Mr. Qureshi swore (incorrectly) in an affidavit delivered to Bay Point in connection with the advance of the Second Mortgage and Mr. Qureshi made an incorrect statement of fact on the face of this $250,000 Second Mortgage instrument to the effect the Selwyn Road property was not a matrimonial home on May 28, 2014,

which was absolutely incorrect Selwyn Road was the Qureshi's matrimonial home from its purchase in July of 2011 until June 30, 2015.

13. Mr. Qureshi sold Selwyn Road on June 30, 2015. The net proceeds resulting from the sale, after encumbrances and expenses had been paid, was $372,177.02 (the "Selwyn Road Net Sale Proceeds").

14. On February 18, 2015, Mrs. Qureshi entered into an Agreement of Purchase and Sale (the "APS") on behalf of herself and Mr. Qureshi with a builder for the purchase of a new home municipally described as 55 Davina Circle ("Davina Circle") in Aurora.

15. The APS set out that two refundable deposits (the "Deposits") aggregating $256,250.00 were payable during the first 60 days after the execution of the APS.

16. Mr. Qureshi arranged to have the Deposits paid to the vendor.

17. Mr. Qureshi directed Client360 to pay the Deposits.

18. Client360 directly or indirectly paid the Deposits.

19. The actual amount of Deposits paid was $256,240.00.

20. Mr. and Mrs. Qureshi completed the transaction set out in the APS on June 30, 2015 when they took title to Davina Circle. They took tide to Davina Circle as joint tenants.

21. On closing, the vendor of Davina Circle credited Mr. and Mrs. Qureshi with the Deposits in the amount of $256,240.00.

22. The Selwyn Road Net Sale Proceeds in the amount of $372,177.02 were used to partially pay the purchase price of Davina Circle on June 30, 2015.

23. Mr. and Mrs. Qureshi mortgaged Davina Road and used the borrowed loan proceeds of $1,902,081.04 to partially pay the purchase price of Davina Circle.

24. Just prior to closing, Mr. Qureshi needed the additional sum of $89,654.80 (the "**Shortfall**") in order to complete the purchase.

25. On June 29, 2015, Mrs. Qureshi's parents provided Client360 with two bank drafts, one in the amount of $60,000 in Canadian funds and the other in the amount of $30,000 in US dollars (in order to assist Mr. and Mrs. Qureshi with their purchase of Davina Circle). The Canadian dollar draft ($60,000) was deposited into Client360's Canadian dollar current account and the US dollar draft ($30,000) was deposited into Client360's US dollar bank account

26. On or about June 30, 2015, Mr. Qureshi provided his real estate lawyer with a bank draft drawn on Client360's Canadian dollar current account in the amount of $89,654.80. This amount was used by Mr. and Mrs. Qureshi to cover the Shortfall.

27. The amount of funds used to purchase Davina Circle less the mortgage proceeds was $718,071.82.

28. Bank of Montreal commenced a lawsuit against Mr. Qureshi, Client360 and Mrs. Qureshi (among others) on September 11, 2015 alleging that Mr. Qureshi and Client360 had committed fraud against it

29. In early 2016, the Canadian Finance & Leasing Association circulated a document entitled "Toronto Police Advisory: Fraud & Money Laundering out of the GTA" in which the Toronto Police warned that Mr. Qureshi

and Client360 were individuals "of concern" with respect to "highly sophisticated and organized fraud/ money laundering operations operating out of the Greater Toronto Area".

30. Mercado Capital Corporation commenced a lawsuit against Mr. Qureshi and Client360 (and others) on March 18, 2016 alleging that Mr. Qureshi and Chent360 had committed fraud against it

31. Mercado Capital Corporation sought a Mareva injunction against Mr. Qureshi which Mr. Qureshi consented to.

32 Polaris Leasing Ltd. commenced a lawsuit against Mr. Qureshi and Client360 (and others) on April 14, 2016 alleging that Mr. Qureshi and Client360 had committed fraud against it

33. Mr. Qureshi departed from Canada in March or April of 2016.

34. Mr. Qureshi left Mrs. Qureshi for another woman in March or April of 2016.

35. Mr. and Mrs. Qureshi became separated in March or April of 2016.

36. The date of Mr. Qureshi's initial bankruptcy event was June 2, 2016, when Mercado Capital Corporation had a Bankruptcy Application issued against Mr. Qureshi

37. Mr. Qureshi was adjudged a bankrupt on July 5, 2016.

38. Pollard & Associates Inc. was appointed by the court to act as the trustee for Mr. Qureshi's estate.

39. Pollard & Associates Inc. has admitted the sum of $4,129,284.89 of unsecured debt owed by Mr. Qureshi's estate as at January 24, 2017.

40. Pollard & Associates Inc. has admitted Mercado Capital Corporation's claim of $1,131,133.59.

41. Mrs. Qureshi and Mr. Qureshi's trustee sold the Davina Circle property on November 28, 2016 for a sale price of $2,838,000.00.

42. The net sale proceeds from the sale of Davina Circle was $696,815.74. The sum of $348,407.87 was paid to Mr. Qureshi's estate.

43. The sum of $323,407.87 is being held by the trustee to the credit of the successful party in this Application pursuant to the 2016 Order of Mr. Justice Newbould.

44. In February of 2017, Mr. Qureshi's passport was cancelled and he was forced to return to Canada.

45. Mr. Qureshi was arrested at the airport upon his return to Canada in February of 2017 and charged with multiple counts of fraud over $5,000.00.

ALL OF WHICH IS RESPECTFULLY SUBMITTED

PAPAZIAN HEISEY MYERS
Per: Michael S. Myers
of Counsel for the Applicant

VEENA POHANI & ASSOCIATES
Per: Veena Pohani
of Counsel for the Respondent,
Hafsa Faisal Qureshi

Graphic 1

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Tab 5

2004 SCC 68, 2004 CSC 68
Supreme Court of Canada

People's Department Stores Ltd. (1992) Inc., Re

2004 CarswellQue 2862, 2004 CarswellQue 2863, 2004 SCC 68, 2004 CSC 68, [2004] 3 S.C.R. 461, [2004] S.C.J. No. 64, 134 A.C.W.S. (3d) 548, 244 D.L.R. (4th) 564, 326 N.R. 267 (Eng.), 326 N.R. 267 (Fr.), 49 B.L.R. (3d) 165, 4 C.B.R. (5th) 215, J.E. 2004-2016, REJB 2004-72160

In the Matter of the Bankruptcy of Peoples Department Stores Inc./Magasins à rayons Peoples inc.

Caron Bélanger Ernst & Young Inc., in its capacity as Trustee to the bankruptcy of Peoples Department Stores Inc./Magasins à rayons Peoples inc. (Appellant) v. Lionel Wise, Ralph Wise and Harold Wise (Respondents) and Chubb Insurance Company of Canada/Compagnie d'assurance Chubb du Canada (Respondent)

Iacobucci, * Major, Bastarache, Binnie, LeBel, Deschamps, Fish JJ.

Heard: May 11, 2004
Judgment: October 29, 2004
Docket: 29682

Proceedings: affirming *People's Department Stores Ltd. (1992) Inc., Re* (2003), 2003 CarswellQue 145, (sub nom. *Peoples Department Stores Inc. (Trustees of) v. Wise)* 224 D.L.R. (4th) 509, [2003] R.J.Q. 796, 41 C.B.R. (4th) 225 (C.A. Que.); reversing *People's Department Stores Ltd. (1992) Inc., Re* (1998), (sub nom. *Peoples Department Stores Inc./Magasin à rayons Peoples inc. (Syndic de))* [1999] R.R.A. 178, 1998 CarswellQue 3442, 23 C.B.R. (4th) 200 (C.S. Que.)

Counsel: Gerald F. Kandestin, Gordon Kugler, Gordon Levine for Appellant
Éric Lalanne, Martin Tétreault for Respondents, Lionel Wise, Ralph Wise, Harold Wise
Ian Rose, Odette Jobin-Laberge for Respondent, Chubb Insurance Company of Canada

Subject: Corporate and Commercial; Insolvency; Income Tax (Federal)

APPEAL by bankruptcy trustee from judgment reported at *People's Department Stores Ltd. (1992) Inc., Re* (2003), 2003 CarswellQue 145, (sub nom. *Peoples Department Stores Inc. (Trustees of) v. Wise)* 224 D.L.R. (4th) 509, [2003] R.J.Q. 796, 41 C.B.R. (4th) 225 (C.A. Que.), allowing appeal by directors of bankrupt corporation from judgment allowing trustee's motion to recover funds of corporation and finding directors personally liable.

POURVOI du syndic de faillite à l'encontre de l'arrêt publié à *People's Department Stores Ltd. (1992) Inc., Re* (2003), 2003 CarswellQue 145, (sub nom. *Peoples Department Stores Inc. (Trustees of) v. Wise)* 224 D.L.R. (4th) 509, [2003] R.J.Q. 796, 41 C.B.R. (4th) 225 (C.A. Qué), qui a accueilli le pourvoi des administrateurs d'une société en faillite à l'encontre du jugement qui avait accueilli la requête en recouvrement des fonds de la société présentée par le syndic et condamné personnellement les administrateurs.

Major, Deschamps JJ.:

I. Introduction

1 The principal question raised by this appeal is whether directors of a corporation owe a fiduciary duty to the corporation's creditors comparable to the statutory duty owed to the corporation. For the reasons that follow, we

conclude that directors owe a duty of care to creditors, but that duty does not rise to a fiduciary duty. We agree with the disposition of the Quebec Court of Appeal. The appeal is therefore dismissed.

2 As a result of the demise in the mid-1990s of two major retail chains in eastern Canada, Wise Stores Inc. ("Wise") and its wholly-owned subsidiary, Peoples Department Stores Inc. ("Peoples"), the indebtedness of a number of Peoples' creditors went unsatisfied. In the wake of the failure of the two chains, Caron Bélanger Ernst & Young Inc., Peoples' trustee in bankruptcy (the "trustee"), brought an action against the directors of Peoples. To address the trustee's claims, the extent of the duties imposed by s. 122(1) of the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 ("CBCA"), upon directors with respect to creditors must be determined; we must also identify the purpose and reach of s. 100 of the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3 ("BIA").

3 In our view, it has not been established that the directors of Peoples violated either the fiduciary duty or the duty of care imposed by s. 122(1) of the CBCA. As for the trustee's submission regarding s. 100 of the BIA, we agree with the Court of Appeal that the consideration received in the impugned transactions was not "conspicuously" less than fair market value. The BIA claim fails on that basis.

II. Background

4 Wise was founded by Alex Wise in 1930 as a small clothing store on St-Hubert Street in Montreal. By 1992, through expansion effected by a mix of internal growth and acquisitions, it had become an enterprise operating at 50 locations with annual sales of approximately $100 million, and it had been listed on the Montreal Stock Exchange in 1986. The stores were, for the most part, located in urban areas in Quebec. The founder's three sons, Lionel, Ralph and Harold Wise (the "Wise brothers"), were majority shareholders, officers, and directors of Wise. Together, they controlled 75 percent of the firm's equity.

5 In 1992, Peoples had been in business continuously in one form or another for 78 years. It had operated as an unincorporated division of Marks & Spencer Canada Inc. ("M & S") until 1991, when it was incorporated as a separate company. M & S itself was wholly owned by the large British firm, Marks & Spencer plc. ("M & S plc."). Peoples' 81 stores were generally located in rural areas, from Ontario to Newfoundland. Peoples had annual sales of about $160 million, but was struggling financially. Its annual losses were in the neighbourhood of $10 million.

6 Wise and Peoples competed with other chains such as Canadian Tire, Greenberg, Hart, K-Mart, M-Stores, Metropolitan Stores, Rossy, Woolco and Zellers. Retail competition in eastern Canada was intense in the early 1990s. In 1992, M-Stores went bankrupt. In 1994, Greenberg and Metropolitan Stores followed M-Stores into bankruptcy. The 1994 entry of Wal-Mart into the Canadian market, with its acquisition of over 100 Woolco stores from Woolworth Canada Inc., exerted significant additional competitive pressure on retail stores.

7 Lionel Wise, the eldest of the three brothers and Wise's executive vice-president, had expressed an interest in acquiring the ailing Peoples chain from M & S as early as 1988. Initially, M & S did not share Wise's interest for the sale, but by late 1991, M & S plc., the British parent company of M & S, had decided to divest itself of all its Canadian operations. At this point, M & S incorporated each of its three Canadian divisions to facilitate the anticipated divestiture thereof.

8 The new-found desire to sell coincided with Wise's previously expressed interest in acquiring its larger rival. Although M & S had initially hoped to sell Peoples for cash to a large firm in a solid financial condition, it was unable to do so. Consequently, negotiations got underway with representatives of Wise. A formal share purchase agreement was drawn up in early 1992 and executed in June 1992, with July 16, 1992 as its closing date.

9 Wise incorporated a company, 2798832 Canada Inc., for the purpose of acquiring all of the issued and outstanding shares of Peoples from M & S. The $27- million share acquisition proceeded as a fully leveraged buyout. The portion of the purchase price attributable to inventory was discounted by 30 percent. The discount was designed to inject equity into Peoples in the fiscal year following the sale and to make use of some of the tax losses that had accumulated in prior years.

10 The amount of the down payment due to M & S at closing, $5 million, was borrowed from the Toronto Dominion Bank (the "TD Bank"). According to the terms of the share purchase agreement, the $22-million balance of the purchase price would be carried by M & S and would be repaid over a period of eight years. Wise guaranteed all of 2798832 Canada Inc.'s obligations pursuant to the terms of the share purchase agreement.

11 To protect its interests, M & S took the assets of Peoples as security (subject to a priority in favour of the TD Bank) and negotiated strict covenants concerning the financial management and operation of the company. Among other requirements, 2798832 Canada Inc. and Wise were obligated to maintain specific financial ratios, and Peoples was not permitted to provide financial assistance to Wise. In addition, the agreement provided that Peoples could not be amalgamated with Wise until the purchase price had been paid. This prohibition was presumably intended to induce Wise to refinance and pay the remainder of the purchase price as early as possible in order to overcome the strict conditions imposed upon it under the share purchase agreement.

12 On January 31, 1993, 2798832 Canada Inc. was amalgamated with Peoples. The new entity retained Peoples' corporate name. Since 2798832 Canada Inc. had been a wholly-owned subsidiary of Wise, upon amalgamation the new Peoples became a subsidiary directly owned and controlled by Wise. The three Wise brothers were Peoples' only directors.

13 Following the acquisition, Wise had attempted to rationalize its operations by consolidating the overlapping corporate functions of Wise and Peoples, and operating as a group. The consolidation of the administration, accounting, advertising and purchasing departments of the two corporations was completed by the fall of 1993. As a consequence of the changes, many of Wise's employees worked for both firms but were paid solely by Wise. The evidence at trial was that because of the tax losses carried-forward by Peoples, it was advantageous for the group to have more expenses incurred by Wise, which, if the group was profitable as a whole, would increase its after-tax profits. Almost from the outset, the joint operation of Wise and Peoples did not function smoothly. Instead of the expected synergies, the consolidation resulted in dissonance.

14 After the acquisition, the total number of buyers for the two companies was nearly halved. The procurement policy at that point required buyers to deal simultaneously with suppliers on behalf of both Peoples and Wise. For the buyers, this nearly doubled their administrative work. Separate invoices were required for purchases made on behalf of Wise and Peoples. These invoices had to be separately entered into the system, tracked and paid.

15 Inventory, too, was separately recorded and tracked in the system. However, the inventory of each company was handled and stored, often unsegregated, in shared warehouse facilities. The main warehouse for Peoples, on Cousens Street in Ville St-Laurent, was maintained for and used by both firms. The Cousens warehouse saw considerable activity, as it was the central distribution hub for both chains. The facility was open 18 hours a day and employed 150 people on two shifts who handled a total of approximately 30,000 cartons daily through 20 loading docks. It was abuzz with activity.

16 Before long, the parallel bookkeeping combined with the shared warehousing arrangements caused serious problems for both Wise and Peoples. The actual situation in the warehouse often did not mirror the reported state of the inventory in the system. The goods of one company were often inextricably commingled and confused with the goods of the other. As a result, the inventory records of both companies were increasingly incorrect. A physical inventory count was conducted to try to rectify the situation, to little avail. Both Wise and Peoples stores experienced numerous shipping disruptions and delays. The situation, already unsustainable, was worsening.

17 In October 1993, Lionel Wise consulted David Clément, Wise's (and, after the acquisition, Peoples') vice-president of administration and finance, in an attempt to find a solution. In January 1994, Clément recommended and the three Wise brothers agreed that they would implement a joint inventory procurement policy (the "new policy") whereby the two firms would divide responsibility for purchasing. Peoples would make all purchases from North American suppliers and Wise would, in turn, make all purchases from overseas suppliers. Peoples would then transfer to Wise what it had

purchased for Wise, charging Wise accordingly, and vice versa. The new policy was implemented on February 1, 1994. It was this arrangement that was later criticized by certain creditors and by the trial judge.

18 Approximately 82 percent of the total inventory of Wise and Peoples was purchased from North American suppliers, which inevitably meant that Peoples would be extending a significant trade credit to Wise. The new policy was known to the directors, but was neither formally implemented in writing nor approved by a board meeting or resolution.

19 On April 27, 1994, Lionel Wise outlined the details of the new policy at a meeting of Wise's audit committee. A partner of Coopers & Lybrand was M & S's representative on Wise's board of directors and a member of the audit committee. He attended the April 27th meeting and raised no objection to the new policy when it was introduced.

20 By June 1994, financial statements prepared to reflect the financial position of Peoples as of April 30, 1994 revealed that Wise owed more than $18 million to Peoples. Approximately $14 million of this amount resulted from a notional transfer of inventory that was cancelled following the period's end. M & S was concerned about the situation and started an investigation, as a result of which M & S insisted that the new procurement policy be rescinded. Wise agreed to M & S's demand but took the position that the former procurement policy could not be reinstated immediately. An agreement was executed on September 27, 1994, effective July 21, 1994, and it provided that the new policy would be abandoned as of January 31, 1995. The agreement also specified that the inventory and records of the two companies would be kept separate, and that the amount owed to Peoples by Wise would not exceed $3 million.

21 Another result of the negotiations was that M & S accepted an increase in the amount of the TD Bank's priority to $15 million and a new repayment schedule for the balance of the purchase price owed to M & S. The parties agreed to revise the schedule to provide for 37 monthly payments beginning in July 1995. Each of the Wise brothers also provided a personal guarantee of $500,000 in favour of M & S.

22 In September 1994, in light of the fragile financial condition of the companies and the competitiveness of the retail market, the TD Bank announced its intention to cease doing business with Wise and Peoples as of the end of December 1994. Following negotiations, however, the bank extended its financial support until the end of July 1995. The Wise brothers promised to extend personal guarantees in favour of the TD Bank, but this did not occur.

23 In December 1994, three days after the Wise brothers presented financial statements showing disappointing results for Peoples in its third fiscal quarter, M & S initiated bankruptcy proceedings against both Wise and Peoples. A notice of intention to make a proposal was filed on behalf of Peoples the same day. Nonetheless, Peoples later consented to the petition by M & S, and both Wise and Peoples were declared bankrupt on January 13, 1995, effective December 9, 1994. The same day, M & S released each of the Wise brothers from their personal guarantees. M & S apparently preferred to proceed with an uncontested petition in bankruptcy rather than attempting to collect on the personal guarantees.

24 The assets of Wise and Peoples were sufficient to cover in full the outstanding debt owed to the TD Bank, satisfy the entire balance of the purchase price owed to M & S, and discharge almost all the landlords' lease claims. The bulk of the unsatisfied claims were those of trade creditors.

25 Following the bankruptcy, Peoples' trustee filed a petition against the Wise brothers. In the petition, the trustee claimed that they had favoured the interests of Wise over Peoples to the detriment of Peoples' creditors, in breach of their duties as directors under s. 122(1) of the CBCA. The trustee also claimed that the Wise brothers had, in the year preceding the bankruptcy, been privy to transactions in which property had been transferred for conspicuously less than fair market value within the meaning of s. 100 of the BIA.

26 Pursuant to art. 2501 of the *Civil Code of Québec*, S.Q. 1991, c. 64 ("C.C.Q."), the trustee named Chubb Insurance Company of Canada ("Chubb"), which had provided directors' insurance to Wise and its subsidiaries, as a defendant in addition to the Wise brothers.

27 The trial judge, Greenberg J., relying on decisions from the United Kingdom, Australia and New Zealand, held that the fiduciary duty and the duty of care under s. 122 (1) of the CBCA extend to a company's creditors when a company is insolvent or in the vicinity of insolvency. Greenberg J. found that the implementation, by the Wise brothers qua directors of Peoples, of a corporate policy that affected both companies, had occurred while the corporation was in the vicinity of insolvency and was detrimental to the interests of the creditors of Peoples. The Wise brothers were therefore found liable and the trustee was awarded $4.44 million in damages. As Chubb had provided insurance coverage for directors, it was also held liable. Greenberg J. also considered the alternative grounds under the BIA advanced by the trustee and found the Wise brothers liable for the same $4.44 million amount on that ground as well. All the parties appealed.

28 The Quebec Court of Appeal, *per* Pelletier J.A., with Robert C.J.Q. and Nuss J.A. concurring, allowed the appeals by Chubb and the Wise brothers. The Court of Appeal expressed reluctance to follow Greenberg J. in equating the interests of creditors with the best interests of the corporation when the corporation was insolvent or in the vicinity of insolvency, stating that an innovation in the law such as this is a policy matter more appropriately dealt with by Parliament than the courts. In considering the trustee's claim under s. 100 of the BIA, Pelletier J.A. held that the trial judge had committed a palpable and overriding error in concluding that the amounts owed by Wise to Peoples in respect of inventory "were neither collected nor collectible". He found that the consideration received for the transactions had been approximately 94 percent of fair market value, and he was not convinced that this disparity could be characterized as being "conspicuously" less than fair market value. Moreover, he did not accept the broad meaning the trial judge gave to the word "privy". Pelletier J.A. declined to exercise his discretion under s. 100(2) of the BIA to make an order in favour of the trustee. In view of his conclusion that the Wise brothers were not liable, Pelletier J.A. allowed the appeal with respect to Chubb.

III. Analysis

29 At the outset, it should be acknowledged that according to art. 300 of the C.C.Q. and s. 8.1 of the *Interpretation Act*, R.S.C. 1985, c. I-21, the civil law serves as a supplementary source of law to federal legislation such as the CBCA. Since the CBCA does not entitle creditors to sue directors directly for breach of their duties, it is appropriate to have recourse to the *Civil Code of Québec* to determine how rights grounded in a federal statute should be addressed in Quebec, and more specifically how s. 122(1) of the CBCA can be harmonized with the principles of civil liability: see R. Crête and S. Rousseau, *Droit des sociétés par actions: principes fondamentaux* (2002), at p. 58.

30 This case came before our Court on the issue of whether directors owe a duty to creditors. The creditors did not bring a derivative action or an oppression remedy application under the CBCA. Instead, the trustee, representing the interests of the creditors, sued the directors for an alleged breach of the duties imposed by s. 122(1) of the CBCA. The standing of the trustee to sue was not questioned.

31 The primary role of directors is described in s. 102(1) of the CBCA:

> **102.** (1) Subject to any unanimous shareholder agreement, the directors shall manage, or supervise the management of, the business and affairs of a corporation.

As for officers, s. 121 of the CBCA provides that their powers are delegated to them by the directors:

> **121.** Subject to the articles, the by-laws or any unanimous shareholder agreement,
>
> (a) the directors may designate the offices of the corporation, appoint as officers persons of full capacity, specify their duties and delegate to them powers to manage the business and affairs of the corporation, except powers to do anything referred to in subsection 115(3);
>
> (b) a director may be appointed to any office of the corporation; and
>
> (c) two or more offices of the corporation may be held by the same person.

Although the shareholders are commonly said to own the corporation, in the absence of a unanimous shareholder agreement to the contrary, s. 102 of the CBCA provides that it is not the shareholders, but the directors elected by the shareholders, who are responsible for managing it. This clear demarcation between the respective roles of shareholders and directors long predates the 1975 enactment of the CBCA: see *Automatic Self Cleansing Filter Syndicate Co. v. Cunninghame*, [1906] 2 Ch. 34 (Eng. Ch.); see also art. 311, C.C.Q.

32 Subsection 122(1) of the CBCA establishes two distinct duties to be discharged by directors and officers in managing, or supervising the management of, the corporation:

> **122.** (1) Every director and officer of a corporation in exercising their powers and discharging their duties shall
>
> (a) act honestly and in good faith with a view to the best interests of the corporation; and
>
> (b) exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances.

The first duty has been referred to in this case as the "fiduciary duty". It is better described as the "duty of loyalty". We will use the expression "statutory fiduciary duty" for purposes of clarity when referring to the duty under the CBCA. This duty requires directors and officers to act honestly and in good faith with a view to the best interests of the corporation. The second duty is commonly referred to as the "duty of care". Generally speaking, it imposes a legal obligation upon directors and officers to be diligent in supervising and managing the corporation's affairs.

33 The trial judge did not apply or consider separately the two duties imposed on directors by s. 122(1). As the Court of Appeal observed, the trial judge appears to have confused the two duties. They are, in fact, distinct and are designed to secure different ends. For that reason, they will be addressed separately in these reasons.

A. The Statutory Fiduciary Duty: Section 122(1)(a) of the CBCA

34 Considerable power over the deployment and management of financial, human, and material resources is vested in the directors and officers of corporations. For the directors of CBCA corporations, this power originates in s. 102 of the Act. For officers, this power comes from the powers delegated to them by the directors. In deciding to invest in, lend to or otherwise deal with a corporation, shareholders and creditors transfer control over their assets to the corporation, and hence to the directors and officers, in the expectation that the directors and officers will use the corporation's resources to make reasonable business decisions that are to the corporation's advantage.

35 The statutory fiduciary duty requires directors and officers to act honestly and in good faith *vis-à-vis* the corporation. They must respect the trust and confidence that have been reposed in them to manage the assets of the corporation in pursuit of the realization of the objects of the corporation. They must avoid conflicts of interest with the corporation. They must avoid abusing their position to gain personal benefit. They must maintain the confidentiality of information they acquire by virtue of their position. Directors and officers must serve the corporation selflessly, honestly and loyally: see K.P. McGuinness, *The Law and Practice of Canadian Business Corporations* (1999), at p. 715.

36 The common law concept of fiduciary duty was considered in *B. (K.L.) v. British Columbia*, [2003] 2 S.C.R. 403, 2003 SCC 51 (S.C.C.). In that case, which involved the relationship between the government and foster children, a majority of this Court agreed with McLachlin C.J. who stated, at paras. 40-41 and 49:

> ...Fiduciary duties arise in a number of different contexts, including express trusts, relationships marked by discretionary power and trust, and the special responsibilities of the Crown in dealing with aboriginal interests....
>
> What ... might the content of the fiduciary duty be if it is understood ... as a private law duty arising simply from the relationship of discretionary power and trust between the Superintendent and the foster children? In *Lac Minerals Ltd. v. International Corona Resources Ltd.*, [1989] 2 S.C.R. 574, at pp. 646-47, La Forest J. noted that there are

> certain common threads running through fiduciary duties that arise from relationships marked by discretionary power and trust, such as loyalty and "the avoidance of a conflict of duty and interest and a duty not to profit at the expense of the beneficiary". However, he also noted that "[t]he obligation imposed may vary in its specific substance depending on the relationship" (p. 646)....
>
> ...concern for the best interests of the child informs the parental fiduciary relationship, as La Forest J. noted in *M. (K.) v. M. (H.), supra*, at p. 65. But the duty imposed is to act loyally, and not to put one's own or others' interests ahead of the child's in a manner that abuses the child's trust.... The parent who exercises undue influence over the child in economic matters for his own gain has put his own interests ahead of the child's, in a manner that abuses the child's trust in him. The same may be said of the parent who uses a child for his sexual gratification or a parent who, wanting to avoid trouble for herself and her household, turns a blind eye to the abuse of a child by her spouse. The parent need not, as the Court of Appeal suggested in the case at bar, be consciously motivated by a desire for profit or personal advantage; nor does it have to be her own interests, rather than those of a third party, that she puts ahead of the child's. It is rather a question of disloyalty -- of putting someone's interests ahead of the child's in a manner that abuses the child's trust. Negligence, even aggravated negligence, will not ground parental fiduciary liability unless it is associated with breach of trust in this sense. [Emphasis added.]

37 The issue to be considered here is the "specific substance" of the fiduciary duty based on the relationship of directors to corporations under the CBCA.

38 It is settled law that the fiduciary duty owed by directors and officers imposes strict obligations: see *Canadian Aero Service Ltd. v. O'Malley* (1973), [1974] S.C.R. 592 (S.C.C.), at pp. 609-10, *per* Laskin J. (as he then was), where it was decided that directors and officers may even have to account to the corporation for profits they make that do not come at the corporation's expense:

> The reaping of a profit by a person at a company's expense while a director thereof is, of course, an adequate ground upon which to hold the director accountable. Yet there may be situations where a profit must be disgorged, although not gained at the expense of the company, on the ground that a director must not be allowed to use his position as such to make a profit even if it was not open to the company, as for example, by reason of legal disability, to participate in the transaction. An analogous situation, albeit not involving a director, existed for all practical purposes in the case of *Phipps v. Boardman* [[1967] 2 A.C. 46], which also supports the view that liability to account does not depend on proof of an actual conflict of duty and self-interest. Another, quite recent, illustration of a liability to account where the company itself had failed to obtain a business contract and hence could not be regarded as having been deprived of a business opportunity is *Industrial Development Consultants Ltd. v. Cooley* [[1972] 2 All E.R. 162], a judgment of a Court of first instance. There, the managing director, who was allowed to resign his position on a false assertion of ill health, subsequently got the contract for himself. That case is thus also illustrative of the situation where a director's resignation is prompted by a decision to obtain for himself the business contract denied to his company and where he does obtain it without disclosing his intention. [Emphasis added.]

A compelling argument for making directors accountable for profits made as a result of their position, though not at the corporation's expense, is presented by J. Brock, "The Propriety of Profitmaking: Fiduciary Duty and Unjust Enrichment" (2000), 58 *U.T. Fac. L. Rev.* 185, at pp. 204-5.

39 However, it is not required that directors and officers in all cases avoid personal gain as a direct or indirect result of their honest and good faith supervision or management of the corporation. In many cases the interests of directors and officers will innocently and genuinely coincide with those of the corporation. If directors and officers are also shareholders, as is often the case, their lot will automatically improve as the corporation's financial condition improves. Another example is the compensation that directors and officers usually draw from the corporations they serve. This benefit, though paid by the corporation, does not, if reasonable, ordinarily place them in breach of their fiduciary duty. Therefore, all the circumstances may be scrutinized to determine whether the directors and officers have acted honestly and in good faith with a view to the best interests of the corporation.

40 In our opinion, the trial judge's determination that there was no fraud or dishonesty in the Wise brothers' attempts to solve the mounting inventory problems of Peoples and Wise stands in the way of a finding that they breached their fiduciary duty. Greenberg J. stated, at para. 180:

> We hasten to add that in the present case, the Wise Brothers derived no direct personal benefit from the new domestic inventory procurement policy, albeit that, as the controlling shareholders of Wise Stores, there was an indirect benefit to them. Moreover, as was conceded by the other parties herein, in deciding to implement the new domestic inventory procurement policy, there was no dishonesty or fraud on their part.

The Court of Appeal relied heavily on this finding by the trial judge, as do we. At para. 84, Pelletier J.A. stated that:

> [TRANSLATION] In regard to fiduciary duty, I would like to point out that the brothers were driven solely by the wish to resolve the problem of inventory procurement affecting both the operations of Peoples Inc. and those of Wise. [This is a] motivation that is in line with the pursuit of the interests of the corporation within the meaning of paragraph 122(1)(*a*) C.B.C.A. and that does not expose them to any justified criticism.

41 As explained above, there is no doubt that both Peoples and Wise were struggling with a serious inventory management problem. The Wise brothers considered the problem and implemented a policy they hoped would solve it. In the absence of evidence of a personal interest or improper purpose in the new policy, and in light of the evidence of a desire to make both Wise and Peoples "better" corporations, we find that the directors did not breach their fiduciary duty under s. 122(1)(*a*) of the CBCA. See *820099 Ontario Inc. v. Harold E. Ballard Ltd.* (1991), 3 B.L.R. (2d) 123 (Ont. Gen. Div.) (aff'd (1991), 3 B.L.R. (2d) 113 (Ont. Div. Ct.)), in which Farley J., at p. 171, correctly observes that in resolving a conflict between majority and minority shareholders, it is safe for directors and officers to act to make the corporation a "better corporation".

42 This appeal does not relate to the non-statutory duty directors owe to shareholders. It is concerned only with the statutory duties owed under the CBCA. Insofar as the statutory fiduciary duty is concerned, it is clear that the phrase the "best interests of the corporation" should be read not simply as the "best interests of the shareholders". From an economic perspective, the "best interests of the corporation" means the maximization of the value of the corporation: see E.M. Iacobucci, "Directors' Duties in Insolvency: Clarifying What Is at Stake" (2003), 39(3) *Can. Bus. L.J.* 398, at pp. 400-1. However, the courts have long recognized that various other factors may be relevant in determining what directors should consider in soundly managing with a view to the best interests of the corporation. For example, in *Teck Corp. v. Millar* (1972), 33 D.L.R. (3d) 288 (B.C. S.C.), Berger J. stated, at p. 314:

> A classical theory that once was unchallengeable must yield to the facts of modern life. In fact, of course, it has. If today the directors of a company were to consider the interests of its employees no one would argue that in doing so they were not acting *bona fide* in the interests of the company itself. Similarly, if the directors were to consider the consequences to the community of any policy that the company intended to pursue, and were deflected in their commitment to that policy as a result, it could not be said that they had not considered bona fide the interests of the shareholders.
>
> I appreciate that it would be a breach of their duty for directors to disregard entirely the interests of a company's shareholders in order to confer a benefit on its employees: *Parke v. Daily News Ltd.*, [1962] Ch. 927. But if they observe a decent respect for other interests lying beyond those of the company's shareholders in the strict sense, that will not, in my view, leave directors open to the charge that they have failed in their fiduciary duty to the company.

The case of *Olympia & York Enterprises Ltd. v. Hiram Walker Resources Ltd.* (1986), 59 O.R. (2d) 254 (Ont. Div. Ct.), approved, at p. 271, the decision in *Teck, supra*. We accept as an accurate statement of law that in determining whether they are acting with a view to the best interests of the corporation it may be legitimate, given all the circumstances of a given case, for the board of directors to consider, inter alia, the interests of shareholders, employees, suppliers, creditors, consumers, governments and the environment.

43 The various shifts in interests that naturally occur as a corporation's fortunes rise and fall do not, however, affect the content of the fiduciary duty under s. 122(1)(*a*) of the CBCA. At all times, directors and officers owe their fiduciary obligation to the corporation. The interests of the corporation are not to be confused with the interests of the creditors or those of any other stakeholders.

44 The interests of shareholders, those of the creditors and those of the corporation may and will be consistent with each other if the corporation is profitable and well capitalized and has strong prospects. However, this can change if the corporation starts to struggle financially. The residual rights of the shareholders will generally become worthless if a corporation is declared bankrupt. Upon bankruptcy, the directors of the corporation transfer control to a trustee, who administers the corporation's assets for the benefit of creditors.

45 Short of bankruptcy, as the corporation approaches what has been described as the "vicinity of insolvency", the residual claims of shareholders will be nearly exhausted. While shareholders might well prefer that the directors pursue high-risk alternatives with a high potential payoff to maximize the shareholders' expected residual claim, creditors in the same circumstances might prefer that the directors steer a safer course so as to maximize the value of their claims against the assets of the corporation.

46 The directors' fiduciary duty does not change when a corporation is in the nebulous "vicinity of insolvency". That phrase has not been defined; moreover, it is incapable of definition and has no legal meaning. What it is obviously intended to convey is a deterioration in the corporation's financial stability. In assessing the actions of directors it is evident that any honest and good faith attempt to redress the corporation's financial problems will, if successful, both retain value for shareholders and improve the position of creditors. If unsuccessful, it will not qualify as a breach of the statutory fiduciary duty.

47 For a discussion of the shifting interests and incentives of shareholders and creditors, see W.D. Gray, "*Peoples v. Wise* and *Dylex*: Identifying Stakeholder Interests upon or near Corporate Insolvency — Stasis or Pragmatism?" (2003), 39 *Can. Bus. L.J.* 242, at p. 257; E. M. Iacobucci & K.E. Davis, "Reconciling Derivative Claims and the Oppression Remedy" (2000), 12 *S.C.L.R.* (2d) 87, at p. 114. In resolving these competing interests, it is incumbent upon the directors to act honestly and in good faith with a view to the best interests of the corporation. In using their skills for the benefit of the corporation when it is in troubled waters financially, the directors must be careful to attempt to act in its best interests by creating a "better" corporation, and not to favour the interests of any one group of stakeholders. If the stakeholders cannot avail themselves of the statutory fiduciary duty (the duty of loyalty, *supra*) to sue the directors for failing to take care of their interests, they have other means at their disposal.

48 The Canadian legal landscape with respect to stakeholders is unique. Creditors are only one set of stakeholders, but their interests are protected in a number of ways. Some are specific, as in the case of amalgamation: s. 185 of the CBCA. Others cover a broad range of situations. The oppression remedy of s. 241(2)(*c*) of the CBCA and the similar provisions of provincial legislation regarding corporations grant the broadest rights to creditors of any common law jurisdiction: see D. Thomson, "Directors, Creditors and Insolvency: A Fiduciary Duty or a Duty Not to Oppress?" (2000), 58(1) *U.T. Fac. L. Rev.* 31, at p. 48. One commentator describes the oppression remedy as "the broadest, most comprehensive and most open-ended shareholder remedy in the common law world": S.M. Beck, "Minority Shareholders' Rights in the 1980s" in *Corporate Law in the 80s* (1982), 311, at p. 312. While Beck was concerned with shareholder remedies, his observation applies equally to those of creditors.

49 The fact that creditors' interests increase in relevancy as a corporation's finances deteriorate is apt to be relevant to, *inter alia*, the exercise of discretion by a court in granting standing to a party as a "complainant" under s. 238(*d*) of the CBCA as a "proper person" to bring a derivative action in the name of the corporation under ss. 239 and 240 of the CBCA, or to bring an oppression remedy claim under s. 241 of the CBCA.

50 Section 241(2)(*c*) authorizes a court to grant a remedy

if the powers of the directors of the corporation or any of its affiliates are or have been exercised in a manner

> that is oppressive or unfairly prejudicial to or that unfairly disregards the interests of any security holder, creditor, director or officer...

A person applying for the oppression remedy must, in the court's opinion, fall within the definition of "complainant" found in s. 238 of the CBCA:

> (a) a registered holder or beneficial owner, and a former registered holder or beneficial owner, of a security of a corporation or any of its affiliates,
>
> (b) a director or an officer or a former director or officer of a corporation or any of its affiliates,
>
> (c) the Director, or
>
> (d) any other person who, in the discretion of a court, is a proper person to make an application under this Part.

Creditors, who are not security holders within the meaning of para. (*a*), may therefore apply for the oppression remedy under para. (*d*) by asking a court to exercise its discretion and grant them status as a "complainant".

51 Section 241 of the CBCA provides a possible mechanism for creditors to protect their interests from the prejudicial conduct of directors. In our view, the availability of such a broad oppression remedy undermines any perceived need to extend the fiduciary duty imposed on directors by s. 122(1)(*a*) of the CBCA to include creditors.

52 The Court of Appeal, at paras. 99-100, referred to *373409 Alberta Ltd. (Receiver of) v. Bank of Montreal*, [2002] 4 S.C.R. 312, 2002 SCC 81 (S.C.C.), as an indication by this Court that the interests of creditors do not have any bearing on the assessment of the conduct of directors. However, the receiver in that case was representing the corporation's rights and not the creditors' rights; therefore, the case has no application in this appeal. *373409 Alberta Ltd.* involved an action taken by the receiver on behalf of the corporation against a bank for the tort of conversion. The sole shareholder, director and officer of 373409 Alberta Ltd., who was also the sole shareholder, director and officer of another corporation, Legacy Holdings Ltd., had deposited a cheque payable to 373409 Alberta Ltd. into the account of Legacy. While it was recognized, at para. 22, that the diversion of money from 373409 Alberta Ltd. to Legacy "may very well have been wrongful vis-à-vis [373409 Alberta Ltd.]'s creditors" (none of whom were involved in the action), no fraud had been committed against the corporation itself and the bank, acting on proper authority, had not wrongfully interfered with the cheque by carrying out the deposit instructions. The statutory duties of the directors were not at issue, nor were they considered, and no assessment of the creditors' rights was made. With respect, Pelletier J.A.'s broad reading of *373409 Alberta Ltd.* was misplaced.

53 In light of the availability both of the oppression remedy and of an action based on the duty of care, which will be discussed below, stakeholders have viable remedies at their disposal. There is no need to read the interests of creditors into the duty set out in s. 122(1)(*a*) of the CBCA. Moreover, in the circumstances of this case, the Wise brothers did not breach the statutory fiduciary duty owed to the corporation.

B. The Statutory Duty of Care: Section 122(1)(b) of the CBCA

54 As mentioned above, the CBCA does not provide for a direct remedy for creditors against directors for breach of their duties and the C.C.Q. is used as suppletive law.

55 In Quebec, directors have been held liable to creditors in respect of either contractual or extra-contractual obligations. Contractual liability arises where the director personally guarantees a contractual obligation of the company. Liability also arises where the director personally acts in a manner that triggers his or her extra-contractual liability. See P. Martel, "Le 'voile corporatif' — l'attitude des tribunaux face à l'article 317 du Code civil du Québec" (1998), 58 R. du

B. 95, at pp. 135-36; *Brasserie Labatt ltée c. Lanoue*, [1999] J.Q. No. 1108 (C.A. Que.), *per* Forget J.A., at para. 29. It is clear that the Wise brothers cannot be held contractually liable as they did not guarantee the debts at issue here. Extra-contractual liability is the remaining possibility.

56 To determine the applicability of extra-contractual liability in this appeal, it is necessary to refer to art. 1457 of the C.C.Q.:

> Every person has a duty to abide by the rules of conduct which lie upon him, according to the circumstances, usage or law, so as not to cause injury to another.
>
> Where he is endowed with reason and fails in this duty, he is responsible for any injury he causes to another person by such fault and is liable to reparation for the injury, whether it be bodily, moral or material in nature.
>
> He is also liable, in certain cases, to reparation for injury caused to another by the act or fault of another person or by the act of things in his custody. [Emphasis added]

Three elements of art. 1457 of the C.C.Q. are relevant to the integration of the director's duty of care into the principles of extra-contractual liability: who has the duty ("every person"), to whom is the duty owed ("another") and what breach will trigger liability ("rules of conduct"). It is clear that directors and officers come within the expression "every person". It is equally clear that the word "another" can include the creditors. The reach of art. 1457 of the C.C.Q. is broad and it has been given an open and inclusive meaning. See *Regent Taxi & Transport Co. v. Congrégation des petits frères de Marie*, [1929] S.C.R. 650 (S.C.C.), *per* Anglin C.J., at p. 655 (rev'd on other grounds, [1932] 2 D.L.R. 70 (Que. K.B.)):

> ...to narrow the prima facie scope of art. 1053 C.C. [now art. 1457] is highly dangerous and would necessarily result in most meritorious claims being rejected; many a wrong would be without a remedy.

This liberal interpretation was also affirmed and treated as settled by this Court in *Lister v. McAnulty*, [1944] S.C.R. 317 (S.C.C.), and *Hôpital Notre-Dame de l'Espérance c. Laurent* (1977), [1978] 1 S.C.R. 605 (S.C.C.).

57 This interpretation can be harmoniously integrated with the wording of the CBCA. Indeed, unlike the statement of the fiduciary duty in s. 122(1)(*a*) of the CBCA, which specifies that directors and officers must act with a view to the best interests of the corporation, the statement of the duty of care in s. 122(1)(*b*) of the CBCA does not specifically refer to an identifiable party as the beneficiary of the duty. Instead, it provides that "[e]very director and officer of a corporation in exercising his powers and discharging his duties shall ... exercise the care, diligence and skill that a reasonably prudent person would exercise in comparable circumstances." Thus, the identity of the beneficiary of the duty of care is much more open-ended, and it appears obvious that it must include creditors. This result is clearly consistent with the civil law interpretation of the word "another". Therefore, if breach of the standard of care, causation and damages are established, creditors can resort to art. 1457 to have their rights vindicated. The only issue thus remaining is the determination of the "rules of conduct" likely to trigger extracontractual liability. On this issue, art. 1457 is explicit.

58 The first paragraph of art. 1457 does not set the standard of conduct. Instead, it incorporates by reference s. 122(1)(*b*) of the CBCA. The statutory duty of care is a "duty to abide by [a rule] of conduct which lie[s] upon [them], according to the ... law, so as not to cause injury to another". Thus, for the purpose of determining whether the Wise brothers can be held liable, only the CBCA is relevant. It is therefore necessary to outline the requirements of the duty of care embodied in s. 122(1)(*b*) of the CBCA.

59 That directors must satisfy a duty of care is a long-standing principle of the common law, although the duty of care has been reinforced by statute to become more demanding. Among the earliest English cases establishing the duty of care were *Dovey v. Cory*, [1901] A.C. 477 (Eng. H.L.); *Brazilian Rubber Plantation & Estates Ltd., Re*, [1911] 1 Ch. 425 (Eng. Ch. Div.); and *City Equitable Fire Insurance Co., Re* (1924), [1925] 1 Ch. 407 (Eng. C.A.). In substance, these cases held that the standard of care was a reasonably relaxed, subjective standard. The common law required directors to avoid being grossly negligent with respect to the affairs of the corporation and judged them according to their own

personal skills, knowledge, abilities and capacities. See McGuinness, *supra*, at p. 776: "Given the history of case law in this area, and the prevailing standards of competence displayed in commerce generally, it is quite clear that directors were not expected at common law to have any particular business skill or judgment".

60 The 1971 report entitled *Proposals for a New Business Corporations Law for Canada* (1971) ("Dickerson Report") culminated the work of a committee headed by R.W. V. Dickerson which had been appointed by the federal government to study the need for new federal business corporations legislation. This report preceded the enactment of the CBCA by four years and influenced the eventual structure of the CBCA.

61 The standard recommended by the Dickerson Report was objective, requiring directors and officers to meet the standard of a "reasonably prudent person" (vol. II, at p. 74):

> **9.19**
>
> (1) Every director and officer of a corporation in exercising his powers and discharging his duties shall
>
> . . . . .
>
> (b) exercise the care, diligence and skill of a reasonably prudent person.

The report described how this proposed duty of care differed from the prevailing common law duty of care (vol. I, at p. 83):

> **242.** The formulation of the duty of care, diligence and skill owed by directors represents an attempt to upgrade the standard presently required of them. The principal change here is that whereas at present the law seems to be that a director is only required to demonstrate the degree of care, skill and diligence that could reasonably be expected from him, having regard to his knowledge and experience -- *Re City Equitable Fire Insurance Co.*, [1925] Ch. 425 -- under s. 9.19(1)(b) he is required to conform to the standard of a reasonably prudent man. Recent experience has demonstrated how low the prevailing legal standard of care for directors is, and we have sought to raise it significantly. We are aware of the argument that raising the standard of conduct for directors may deter people from accepting directorships. The truth of that argument has not been demonstrated and we think it is specious. The duty of care imposed by s. 9.19(1)(b) is exactly the same as that which the common law imposes on every professional person, for example, and there is no evidence that this has dried up the supply of lawyers, accountants, architects, surgeons or anyone else. It is in any event cold comfort to a shareholder to know that there is a steady supply of marginally competent people available under present law to manage his investment. [Emphasis added.]

62 The statutory duty of care in s. 122(1)(*b*) of the CBCA emulates but does not replicate the language proposed by the Dickerson Report. The main difference is that the enacted version includes the words "in comparable circumstances", which modifies the statutory standard by requiring the context in which a given decision was made to be taken into account. This is not the introduction of a subjective element relating to the competence of the director, but rather the introduction of a contextual element into the statutory standard of care. It is clear that s. 122(1)(*b*) requires more of directors and officers than the traditional common law duty of care outlined in, for example, *City Equitable Fire Insurance Co., Re*, *supra*.

63 The standard of care embodied in s. 122(1)(*b*) of the CBCA was described by Robertson J.A. of the Federal Court of Appeal in *Soper v. R.* (1997), [1998] 1 F.C. 124 (Fed. C.A.), at para. 41, as being "objective subjective". Although that case concerned the interpretation of a provision of the *Income Tax Act*, it is relevant here because the language of the provision establishing the standard of care was identical to that of s. 122(1)(*b*) of the CBCA. With respect, we feel that Robertson J.A.'s characterization of the standard as an "objective subjective" one could lead to confusion. We prefer to describe it as an objective standard. To say that the standard is objective makes it clear that the factual aspects of the circumstances surrounding the actions of the director or officer are important in the case of the s. 122(1)(*b*) duty of care,

as opposed to the subjective motivation of the director or officer, which is the central focus of the statutory fiduciary duty of s. 122(1)(*a*) of the CBCA.

64 The contextual approach dictated by s.122(1)(*b*) of the CBCA not only emphasizes the primary facts but also permits prevailing socio-economic conditions to be taken into consideration. The emergence of stricter standards puts pressure on corporations to improve the quality of board decisions. The establishment of good corporate governance rules should be a shield that protects directors from allegations that they have breached their duty of care. However, even with good corporate governance rules, directors' decisions can still be open to criticism from outsiders. Canadian courts, like their counterparts in the United States, the United Kingdom, Australia and New Zealand, have tended to take an approach with respect to the enforcement of the duty of care that respects the fact that directors and officers often have business expertise that courts do not. Many decisions made in the course of business, although ultimately unsuccessful, are reasonable and defensible at the time they are made. Business decisions must sometimes be made, with high stakes and under considerable time pressure, in circumstances in which detailed information is not available. It might be tempting for some to see unsuccessful business decisions as unreasonable or imprudent in light of information that becomes available *ex post facto*. Because of this risk of hindsight bias, Canadian courts have developed a rule of deference to business decisions called the "business judgment rule", adopting the American name for the rule.

65 In *Pente Investment Management Ltd. v. Schneider Corp.* (1998), 42 O.R. (3d) 177 (Ont. C.A.), Weiler J.A. stated, at p. 192:

> The law as it has evolved in Ontario and Delaware has the common requirements that the court must be satisfied that the directors have acted reasonably and fairly. <u>The court looks to see that the directors made a *reasonable* decision *not a perfect* decision. Provided the decision taken is within a range of reasonableness, the court ought not to substitute its opinion for that of the board even though subsequent events may have cast doubt on the board's determination.</u> As long as the directors have selected one of several reasonable alternatives, deference is accorded to the board's decision [references omitted]. This formulation of deference to the decision of the Board is known as the "business judgment rule". The fact that alternative transactions were rejected by the directors is irrelevant unless it can be shown that a particular alternative was definitely available and clearly more beneficial to the company than the chosen transaction
>
> [reference omitted]. [Emphasis added; italics in original.]

66 In order for a plaintiff to succeed in challenging a business decision he or she has to establish that the directors acted (i) in breach of the duty of care and (ii) in a way that caused injury to the plaintiff: W.T. Allen, J.B. Jacobs, and L.E. Strine, Jr., "Function Over Form: A Reassessment of Standards of Review in Delaware Corporation Law" (2001), 26 *Del. J. Corp. L.* 859, at p. 892.

67 Directors and officers will not be held to be in breach of the duty of care under s. 122(1)(*b*) of the CBCA if they act prudently and on a reasonably informed basis. The decisions they make must be reasonable business decisions in light of all the circumstances about which the directors or officers knew or ought to have known. In determining whether directors have acted in a manner that breached the duty of care, it is worth repeating that perfection is not demanded. Courts are ill-suited and should be reluctant to second-guess the application of business expertise to the considerations that are involved in corporate decision making, but they are capable, on the facts of any case, of determining whether an appropriate degree of prudence and diligence was brought to bear in reaching what is claimed to be a reasonable business decision at the time it was made.

68 The trustee alleges that the Wise brothers breached their duty of care under s. 122(1)(*b*) of the CBCA by implementing the new procurement policy to the detriment of Peoples' creditors. After considering all the evidence, we agree with the Court of Appeal that the implementation of the new policy was a reasonable business decision that was made with a view to rectifying a serious and urgent business problem in circumstances in which no solution may have

been possible. The trial judge's conclusion that the new policy led inexorably to Peoples' failure and bankruptcy was factually incorrect and constituted a palpable and overriding error.

69 In fact, as noted by Pelletier J.A., there were many factors other than the new policy that contributed more directly to Peoples' bankruptcy. Peoples had lost $10 million annually while being operated by M & S. Wise, which was only marginally profitable and solvent with annual sales of $100 million (versus $160 million for Peoples), had hoped to improve the performance of its new acquisition. Given that the transaction was a fully leveraged buyout, for Wise and Peoples to succeed, Peoples' performance needed to improve dramatically. Unfortunately for both Wise and Peoples, the retail market in eastern Canada had become very competitive in the early 1990s, and this trend continued with the arrival of Wal-Mart in 1994. At paras. 153 and 155, Pelletier J.A. stated:

> [TRANSLATION] In reality, it was that particularly unfavourable financial situation in which the two corporations found themselves that caused their downfall, and it was M. & S. that, to protect its own interests, sounded the charge in December, rightly or wrongly judging that Peoples Inc.'s situation would only worsen over time. It is crystal-clear that the bankruptcy occurred at the most propitious time for M. & S.'s interests, when inventories were high and suppliers were unpaid. In fact, M. & S. recovered the entire balance due on the selling price and almost all of the other debts it was owed.
>
> . . . . .
>
> ...the trial judge did not take into account the fact that the brothers derived no direct benefit from the transaction impugned, that they acted in good faith and that their true intention was to find a solution to the serious inventory management problem that each of the two corporations was facing. Because of an assessment error, he also ignored the fact that Peoples Inc. received a sizable [sic]consideration for the goods it delivered to Wise. Lastly, I note that the act for which the brothers were found liable, i.e. <u>the adoption of a new joint inventory procurement policy, is not as serious as the trial judge made it out to be and that, in opposition to his view, the act was also not the true cause of the bankruptcy of Peoples Inc.</u> [Emphasis added.]

70 The Wise brothers treated the implementation of the new policy as a decision made in the ordinary course of business and, while no formal agreement evidenced the arrangement, a monthly record was made of the inventory transfers. Although this may appear to be a loose business practice, by the autumn of 1993, Wise had already consolidated several aspects of the operations of the two companies. Legally they were two separate entities. However, the financial fate of the two companies had become intertwined. In these circumstances, there was little or no economic incentive for the Wise brothers to jeopardize the interests of Peoples in favour of the interests of Wise. In fact, given the tax losses that Peoples had carried forward, the companies had every incentive to keep Peoples profitable in order to reduce their combined tax liabilities.

71 Arguably, the Wise brothers could have been more precise in pursuing a resolution to the intractable inventory management problems, having regard to all the troublesome circumstances involved at the time the new policy was implemented. But we, like the Court of Appeal, are not satisfied that the adoption of the new policy breached the duty of care under s. 122(1)(*b*) of the CBCA. The directors cannot be held liable for a breach of their duty of care in respect of the creditors of Peoples.

72 The Court of Appeal relied on two additional provisions of the CBCA that in its view could rescue the Wise brothers from a finding that they breached the duty of care: ss. 44(2) and 123(4).

73 Section 44 of the CBCA, which was in force at the time of the impugned transactions but has since been repealed, permitted a wholly-owned subsidiary to give financial assistance to its holding body corporate:

> **44.**(1) Subject to subsection (2), a corporation or any corporation with which it is affiliated shall not, directly or indirectly, give financial assistance by means of a loan, guarantee or otherwise
>
> . . . . .
>
> (2) A corporation may give financial assistance by means of a loan, guarantee or otherwise

. . . . .

(c) to a holding body corporate if the corporation is a wholly-owned subsidiary of the holding body corporate;

74 While s. 44(2) as it then read qualified the prohibition under s. 44(1), it did not serve to supplant the duties of the directors under s. 122(1) of the CBCA. The Court of Appeal erred in concluding that s. 44(2) served as a blanket legitimization of financial assistance given by wholly-owned subsidiaries to parent corporations. In our opinion, it is incumbent upon directors and officers to exercise their powers in conformity with the duties of s. 122(1).

75 Although s. 44(2) authorized certain forms of financial assistance between corporations, this cannot exempt directors and officers from potential liability under s. 122(1) for any financial assistance given by subsidiaries to the parent corporation.

76 When faced with the serious inventory management problem, the Wise brothers sought the advice of the vice-president of finance, David Clément. The Wise brothers claimed as an additional argument that in adopting the solution proposed by Clément, they were relying in good faith on the judgment of a person whose profession lent credibility to his statement, in accordance with the defence provided for in s. 123(4)(*b*) (now s. 123(5)) of the CBCA. The Court of Appeal accepted the argument. We disagree.

77 The reality that directors cannot be experts in all aspects of the corporations they manage or supervise shows the relevancy of a provision such as s. 123(4)(*b*). At the relevant time, the text of s. 123(4) read:

123. ...

. . . . .

(4) A director is not liable under section 118, 119 or 122 if he relies in good faith on

(a) financial statements of the corporation represented to him by an officer of the corporation or in a written report of the auditor of the corporation fairly to reflect the financial condition of the corporation; or

(b) a report of a lawyer, accountant, engineer, appraiser or other person whose profession lends credibility to a statement made by him.

78 Although Clément did have a bachelor's degree in commerce and 15 years of experience in administration and finance with Wise, this experience does not correspond to the level of professionalism required to allow the directors to rely on his advice as a bar to a suit under the duty of care. The named professional groups in s. 123(4)(*b*) were lawyers, accountants, engineers, and appraisers. Clément was not an accountant, was not subject to the regulatory overview of any professional organization and did not carry independent insurance coverage for professional negligence. The title of vice-president of finance should not automatically lead to a conclusion that Clément was a person "whose profession lends credibility to a statement made by him." It is noteworthy that the word "profession" is used, not "position". Clément was simply a non-professional employee of Wise. His judgment on the appropriateness of the solution to the inventory management problem must be regarded in that light. Although we might accept for the sake of argument that Clément was better equipped and positioned than the Wise brothers to devise a plan to solve the inventory management problems, this is not enough. Therefore, in our opinion, the Wise brothers cannot successfully invoke the defence provided by s. 123(4)(*b*) of the CBCA but must rely on the other defences raised.

C. The Claim under Section 100 of the BIA

79 The trustee also claimed against the Wise brothers under s. 100 of the BIA. That section reads:

100.(1) Where a bankrupt sold, purchased, leased, hired, supplied or received property or services in a reviewable transaction within the period beginning on the day that is one year before the date of the initial bankruptcy event and ending on the date of the bankruptcy, both dates included, the court may, on the application of the trustee, inquire into whether the bankrupt gave or received, as the case may be, fair market value in consideration for the property or services concerned in the transaction.

(2) Where the court in proceedings under this section finds that the consideration given or received by the bankrupt in the reviewable transaction was conspicuously greater or less than the fair market value of the property or services concerned in the transaction, the court may give judgment to the trustee against the other party to the transaction, against any other person being privy to the transaction with the bankrupt or against all those persons for the difference between the actual consideration given or received by the bankrupt and the fair market value, as determined by the court, of the property or services concerned in the transaction.

80 The provision has two principal elements. First, subs. (1) requires the transaction to have been conducted within the year preceding the date of bankruptcy. Second, subs. (2) requires that the consideration given or received by the bankrupt be "conspicuously greater or less" than the fair market value of the property concerned.

81 The word "may" is found in both ss. 100(1) and 100(2) of the BIA with respect to the jurisdiction of the court. In *Standard Trustco Ltd. (Trustee of) v. Standard Trust Co.* (1995), 26 O.R. (3d) 1 (Ont. C.A.), a majority of the Ontario Court of Appeal held that, even if the necessary preconditions are present, the exercise of jurisdiction under s. 100(1) to inquire into the transaction, and under s. 100(2) to grant judgment, is discretionary. Equitable principles guide the exercise of discretion. We agree.

82 Referring to s. 100(2) of the BIA, in *Standard Trustco, supra*, at p. 23, Weiler J.A. explained that:

> When a contextual approach is adopted it is apparent that although the conditions of the section have been satisfied the court is not obliged to grant judgment. The court has a residual discretion to exercise. The contextual approach indicates that the good faith of the parties, the intention with which the transaction took place, and whether fair value was given and received in the transaction are important considerations as to whether that discretion should be exercised.

We agree with Weiler J.A. and adopt her position; however, this appeal does not turn on the discretion to ultimately impose liability. In our view, the Court of Appeal did not interfere with the trial judge's exercise of discretion in reviewing the facts and finding a palpable and overriding error.

83 Within the year preceding the date of bankruptcy, Peoples had transferred inventory to Wise for which the trustee claimed Peoples had not received fair market value in consideration. The relevant transactions involved, for the most part, transfers completed in anticipation of the busy holiday season. Given the non-arm's length relationship between Wise and its wholly-owned subsidiary Peoples, there is no question that these inventory transfers could have constituted reviewable transactions.

84 We share the view of the Court of Appeal that it is not only the final transfers that should be considered. In fairness, the inventory transactions should be considered over the entire period from February to December 1994, which was the period when the new policy was in effect.

85 In *Skalbania (Trustee of) v. Wedgewood Village Estates Ltd.* (1989), 37 B.C.L.R. (2d) 88 (B.C. C.A.), the test for determining whether the difference in consideration is "conspicuously greater or less" was held to be not whether it is conspicuous to the parties at the time of the transaction, but whether it is conspicuous to the court having regard to all the relevant factors. This is a sound approach. In that case, a difference of $1.18 million between fair market value and the consideration received by the bankrupt was seen as conspicuous, where the fair market value was $6.6 million, leaving a discrepancy of more than 17 percent. While there is no particular percentage that definitively sets the threshold for a conspicuous difference, the percentage difference is a factor.

86 As for the factors that would be relevant to this determination, the court might consider, inter alia: evidence of the margin of error in valuing the types of assets in question; any appraisals made of the assets in question and evidence of the parties' honestly held beliefs regarding the value of the assets in question; and other circumstances adduced in evidence by the parties to explain the difference between the consideration received and fair market value: see L.W. Houlden and G.B. Morawetz, *Bankruptcy and Insolvency Law of Canada* (3rd ed. (loose-leaf)), vol. 2, at p. 4-114.1.

87 Over the lifespan of the new policy, Peoples transferred to Wise inventory valued at $71.54 million. As of the date of bankruptcy, it had received $59.50 million in property or money from Wise. As explained earlier, the trial judge adjusted the outstanding difference down to a balance of $4.44 million after taking into account, *inter alia*, the reallocation of general and administrative expenses, and adjustments necessitated by imported inventory transferred from Wise to Peoples. Neither party disputed these figures before this Court. We agree with the Court of Appeal's observation that these findings directly conflict with the trial judge's assertion that Peoples had received no consideration for the inventory transfers on the basis that the outstanding accounts were "neither collected nor collectible" from Wise. Like Pelletier J.A., we conclude that the trial judge's finding in this regard was a palpable and overriding error, and we adopt the view of the Court of Appeal.

88 We are not satisfied that, with regard to all the circumstances of this case, a disparity of slightly more than six percent between fair market value and the consideration received constitutes a "conspicuous" difference within the meaning of s. 100(2) of the BIA. Accordingly, we hold that the trustee's claim under the BIA also fails.

89 In addition to permitting the court to give judgment against the other party to the transaction, s. 100(2) of the BIA also permits it to give judgment against someone who was not a party but was "privy" to the transaction. Given our finding that the consideration for the impugned transactions was not "conspicuously less" than fair market value, there is no need to consider whether the Wise brothers would have been "privy" to the transaction for the purpose of holding them liable under s. 100(2). Nonetheless, the disagreement between the trial judge and the Court of Appeal on the interpretation of "privy" in s. 100(2) of the BIA warrants the following observations.

90 The trial judge in this appeal had little difficulty finding that the Wise brothers were privy to the transaction within the meaning of s. 100(2). Pelletier J.A., however, preferred a narrow construction in finding that the Wise brothers were not privy to the transactions. He held, at para. 136, that:

> [TRANSLATION] ... the legislator wanted to provide for the case in which a person other than the co-contracting party of the bankrupt actually received all or part of the benefit resulting from the lack of equality between the respective considerations.

To support this direct benefit requirement, Pelletier J.A. also referred to the French version which uses the term *ayant intérêt*. While he conceded that the respondent brothers received an indirect benefit from the inventory transfers as shareholders of Wise, Pelletier J.A. found this too remote to be considered "privy" to the transactions (paras. 140-41).

91 The primary purpose of s. 100 of the BIA is to reverse the effects of a transaction that stripped value from the estate of a bankrupt person. It makes sense to adopt a more inclusive understanding of the word "privy" to prevent someone who might receive indirect benefits to the detriment of a bankrupt's unsatisfied creditors from frustrating the provision's remedial purpose. The word "privy" should be given a broad reading to include those who benefit directly or indirectly from and have knowledge of a transaction occurring for less than fair market value. In our opinion, this rationale is particularly apt when those who benefit are the controlling minds behind the transaction.

92 A finding that a person was "privy" to a reviewable transaction does not of course necessarily mean that the court will exercise its discretion to make a remedial order against that person. For liability to be imposed, it must be established that the transaction occurred: (a) within the past year; (b) for consideration conspicuously greater or less than fair market value; (c) with the person's knowledge; and (d) in a way that directly or indirectly benefited the person. In addition, after having considered the context and all the above factors, the judge must conclude that the case is a

proper one for holding the person liable. In light of these conditions and of the discretion exercised by the judge, we find that a broad reading of "privy" is appropriate.

IV. Disposition

93 For the foregoing reasons, we would dismiss the appeal with costs to the respondents.

Appeal dismissed.

Pourvoi rejeté.

Footnotes

* Iacobucci J. took no part in the judgment.

End of Document

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 TORONTO MANAGEMENT INC., URBANCORP TORONTO MANAGEMENT INC., URBANCORP (ST. CLAIR VILLAGE) INC., URBANCORP (PATRICIA) INC., URBANCORP (MALLOW) INC., URBANCORP (LAWRENCE) INC., URBANCORP DOWNSVIEW PARK DEVELOPMENT INC., URBANCORP (952 QUEEN WEST) INC., KING RESIDENTIAL INC., URBANCORP 60 ST. CLAIR INC., HIGH RES. INC., BRIDGE ON KING INC. (COLLECTIVELY, THE "APPLICANTS") AND THE AFFILIATED ENTITIES LISTED IN SCHEDULE "A" HERETO

Court of Appeal File No: M49270
Court File No. CV-16-11389-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
(COMMERCIAL LIST)

PROCEEDING COMMENCED IN TORONTO

BOOK OF AUTHORITIES OF SPEEDY ELECTRICAL CONTRACTORS LTD.
(Motion For Leave to Appeal)

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