S.C.C. File No.
(C52187 & C52346)

IN THE SUPREME COURT OF CANADA
(APPLICATION FOR LEAVE TO APPEAL FROM THE COURT OF APPEAL FOR ONTARIO)

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

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF INDALEX LIMITED, INDALEX HOLDINGS (B.C.) LTD., 6326765 CANADA INC. AND NOVAR INC.

B E T W E E N :

SUN INDALEX FINANCE, LLC

APPLICANT
(Respondent)

- and -

UNITED STEELWORKERS, KEITH CARRUTHERS, LEON KOZIEROK, RICHARD BENSON, JOHN FAVERI, KEN WLADRON, JOHN (JACK) W. ROONEY, BERTRAM MCBRIDE, MAX DEGEN, EUGENE D'IORIO, NEIL FRASER, RICHARD SMITH, ROBERT LECKIE, FRED GRANVILLE, GEORGE L. MILLER, THE CHAPTER 7 TRUSTEE OF THE BANKRUPTCY ESTATES OF THE US INDALEX DEBTORS, and THE MONITOR, FTI CONSULTING CANADA ULC

RESPONDENTS
(Appellants/Respondents)

- and -

MORNEAU SOBECO LIMITED PARTNERSHIP and THE SUPERINTENDENT OF FINANCIAL SERVICES

INTERVENERS
(Interveners)

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Ted Leroy Trucking [Century Services] Ltd., Re

Century Services Inc. (Appellant) and Attorney General of Canada on behalf of Her Majesty The Queen in Right of Canada (Respondent)

Supreme Court of Canada

Deschamps J., McLachlin C.J.C., Binnie, LeBel, Fish, Abella, Charron, Rothstein, Cromwell JJ.

Heard: May 11, 2010
Judgment: December 16, 2010
Docket: 33239

Proceedings: reversing *Ted Leroy Trucking Ltd., Re* (2009), 2009 CarswellBC 1195, 2009 G.T.C. 2020 (Eng.), 2009 BCCA 205, 270 B.C.A.C. 167, 454 W.A.C. 167, [2009] 12 W.W.R. 684, 98 B.C.L.R. (4th) 242, [2009] G.S.T.C. 79 (B.C. C.A.); reversing *Ted Leroy Trucking Ltd., Re* (2008), 2008 CarswellBC 2895, 2008 BCSC 1805, [2008] G.S.T.C. 221, 2009 G.T.C. 2011 (Eng.) (B.C. S.C. [In Chambers])

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Subject: Estates and Trusts; Goods and Services Tax (GST); Tax — Miscellaneous; Insolvency

Tax --- Goods and Services Tax — Collection and remittance — GST held in trust

Debtor owed Crown under Excise Tax Act (ETA) for unremitted GST — Debtor sought relief under Companies' Creditors Arrangement Act (CCAA) — Under order of BC Supreme Court, amount of GST debt was placed in trust account and remaining proceeds of sale of assets paid to major secured creditor — Debtor's application for partial lifting of stay of proceedings to assign itself into bankruptcy was granted, while Crown's application for payment of tax debt was dismissed — Crown's appeal to BC Court of Appeal was allowed — Creditor appealed to Supreme Court of Canada — Appeal allowed — Analysis of ETA and CCAA yielded conclusion that CCAA provides that statutory deemed trusts do not apply, and that Parliament did not intend to restore Crown's deemed trust priority in GST claims under CCAA when it amended ETA in 2000 — Parliament had moved away from asserting priority for Crown claims under both CCAA and Bankruptcy and Insolvency Act (BIA), and neither

(2) Did the court exceed its *CCAA* authority by lifting the stay to allow the debtor to make an assignment in bankruptcy?

(3) Did the court's order of April 29, 2008 requiring segregation of the Crown's GST claim in the Monitor's trust account create an express trust in favour of the Crown in respect of those funds?

3. Analysis

10 The first issue concerns Crown priorities in the context of insolvency. As will be seen, the *ETA* provides for a deemed trust in favour of the Crown in respect of GST owed by a debtor "[d]espite ... any other enactment of Canada (except the *Bankruptcy and Insolvency Act*)" (s. 222(3)), while the *CCAA* stated at the relevant time that "notwithstanding any provision in federal or provincial legislation that has the effect of deeming property to be held in trust for Her Majesty, property of a debtor company shall not be [so] regarded" (s. 18.3(1)). It is difficult to imagine two statutory provisions more apparently in conflict. However, as is often the case, the apparent conflict can be resolved through interpretation.

11 In order to properly interpret the provisions, it is necessary to examine the history of the *CCAA*, its function amidst the body of insolvency legislation enacted by Parliament, and the principles that have been recognized in the jurisprudence. It will be seen that Crown priorities in the insolvency context have been significantly pared down. The resolution of the second issue is also rooted in the context of the *CCAA*, but its purpose and the manner in which it has been interpreted in the case law are also key. After examining the first two issues in this case, I will address Tysoe J.A.'s conclusion that an express trust in favour of the Crown was created by the court's order of April 29, 2008.

3.1 Purpose and Scope of Insolvency Law

12 Insolvency is the factual situation that arises when a debtor is unable to pay creditors (see generally, R. J. Wood, *Bankruptcy and Insolvency Law* (2009), at p. 16). Certain legal proceedings become available upon insolvency, which typically allow a debtor to obtain a court order staying its creditors' enforcement actions and attempt to obtain a binding compromise with creditors to adjust the payment conditions to something more realistic. Alternatively, the debtor's assets may be liquidated and debts paid from the proceeds according to statutory priority rules. The former is usually referred to as reorganization or restructuring while the latter is termed liquidation.

13 Canadian commercial insolvency law is not codified in one exhaustive statute. Instead, Parliament has enacted multiple insolvency statutes, the main one being the *BIA*. The *BIA* offers a self-contained legal regime providing for both reorganization and liquidation. Although bankruptcy legislation has a long history, the *BIA* itself is a fairly recent statute — it was enacted in 1992. It is characterized by a rules-based approach to proceedings. The *BIA* is available to insolvent debtors owing $1000 or more, regardless of whether they are natural or legal persons. It contains mechanisms for debtors to make proposals to their creditors for the adjustment of debts. If a proposal fails, the *BIA* contains a bridge to bankruptcy whereby the debtor's assets are liquidated and the proceeds paid to creditors in accordance with the statutory scheme of distribution.

14 Access to the *CCAA* is more restrictive. A debtor must be a company with liabilities in excess of $5 million. Unlike the *BIA*, the *CCAA* contains no provisions for liquidation of a debtor's assets if reorganization fails. There are three ways of exiting *CCAA* proceedings. The best outcome is achieved when the stay of proceedings provides the debtor with some breathing space during which solvency is restored and the *CCAA* process termin-

ates without reorganization being needed. The second most desirable outcome occurs when the debtor's compromise or arrangement is accepted by its creditors and the reorganized company emerges from the *CCAA* proceedings as a going concern. Lastly, if the compromise or arrangement fails, either the company or its creditors usually seek to have the debtor's assets liquidated under the applicable provisions of the *BIA* or to place the debtor into receivership. As discussed in greater detail below, the key difference between the reorganization regimes under the *BIA* and the *CCAA* is that the latter offers a more flexible mechanism with greater judicial discretion, making it more responsive to complex reorganizations.

15 As I will discuss at greater length below, the purpose of the *CCAA* — Canada's first reorganization statute — is to permit the debtor to continue to carry on business and, where possible, avoid the social and economic costs of liquidating its assets. Proposals to creditors under the *BIA* serve the same remedial purpose, though this is achieved through a rules-based mechanism that offers less flexibility. Where reorganization is impossible, the *BIA* may be employed to provide an orderly mechanism for the distribution of a debtor's assets to satisfy creditor claims according to predetermined priority rules.

16 Prior to the enactment of the *CCAA* in 1933 (S.C. 1932-33, c. 36), practice under existing commercial insolvency legislation tended heavily towards the liquidation of a debtor company (J. Sarra, *Creditor Rights and the Public Interest: Restructuring Insolvent Corporations* (2003), at p. 12). The battering visited upon Canadian businesses by the Great Depression and the absence of an effective mechanism for reaching a compromise between debtors and creditors to avoid liquidation required a legislative response. The *CCAA* was innovative as it allowed the insolvent debtor to attempt reorganization under judicial supervision outside the existing insolvency legislation which, once engaged, almost invariably resulted in liquidation (*Reference re Companies' Creditors Arrangement Act (Canada)*, [1934] S.C.R. 659 (S.C.C.), at pp. 660-61; Sarra, *Creditor Rights*, at pp. 12-13).

17 Parliament understood when adopting the *CCAA* that liquidation of an insolvent company was harmful for most of those it affected — notably creditors and employees — and that a workout which allowed the company to survive was optimal (Sarra, *Creditor Rights*, at pp. 13-15).

18 Early commentary and jurisprudence also endorsed the *CCAA's* remedial objectives. It recognized that companies retain more value as going concerns while underscoring that intangible losses, such as the evaporation of the companies' goodwill, result from liquidation (S. E. Edwards, "Reorganizations Under the Companies' Creditors Arrangement Act" (1947), 25 *Can. Bar Rev.* 587, at p. 592). Reorganization serves the public interest by facilitating the survival of companies supplying goods or services crucial to the health of the economy or saving large numbers of jobs (*ibid.*, at p. 593). Insolvency could be so widely felt as to impact stakeholders other than creditors and employees. Variants of these views resonate today, with reorganization justified in terms of rehabilitating companies that are key elements in a complex web of interdependent economic relationships in order to avoid the negative consequences of liquidation.

19 The *CCAA* fell into disuse during the next several decades, likely because amendments to the Act in 1953 restricted its use to companies issuing bonds (S.C. 1952-53, c. 3). During the economic downturn of the early 1980s, insolvency lawyers and courts adapting to the resulting wave of insolvencies resurrected the statute and deployed it in response to new economic challenges. Participants in insolvency proceedings grew to recognize and appreciate the statute's distinguishing feature: a grant of broad and flexible authority to the supervising court to make the orders necessary to facilitate the reorganization of the debtor and achieve the *CCAA's* objectives. The manner in which courts have used *CCAA* jurisdiction in increasingly creative and flexible ways is ex-

plored in greater detail below.

20 Efforts to evolve insolvency law were not restricted to the courts during this period. In 1970, a government-commissioned panel produced an extensive study recommending sweeping reform but Parliament failed to act (see *Bankruptcy and Insolvency: Report of the Study Committee on Bankruptcy and Insolvency Legislation* (1970)). Another panel of experts produced more limited recommendations in 1986 which eventually resulted in enactment of the *Bankruptcy and Insolvency Act* of 1992 (S.C. 1992, c. 27) (see *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* (1986)). Broader provisions for reorganizing insolvent debtors were then included in Canada's bankruptcy statute. Although the 1970 and 1986 reports made no specific recommendations with respect to the *CCAA*, the House of Commons committee studying the *BIA*'s predecessor bill, C-22, seemed to accept expert testimony that the *BIA*'s new reorganization scheme would shortly supplant the *CCAA*, which could then be repealed, with commercial insolvency and bankruptcy being governed by a single statute (*Minutes of Proceedings and Evidence of the Standing Committee on Consumer and Corporate Affairs and Government Operations*, Issue No. 15, October 3, 1991, at pp. 15:15-15:16).

21 In retrospect, this conclusion by the House of Commons committee was out of step with reality. It overlooked the renewed vitality the *CCAA* enjoyed in contemporary practice and the advantage that a flexible judicially supervised reorganization process presented in the face of increasingly complex reorganizations, when compared to the stricter rules-based scheme contained in the *BIA*. The "flexibility of the *CCAA* [was seen as] a great benefit, allowing for creative and effective decisions" (Industry Canada, Marketplace Framework Policy Branch, *Report on the Operation and Administration of the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act* (2002), at p. 41). Over the past three decades, resurrection of the *CCAA* has thus been the mainspring of a process through which, one author concludes, "the legal setting for Canadian insolvency restructuring has evolved from a rather blunt instrument to one of the most sophisticated systems in the developed world" (R. B. Jones, "The Evolution of Canadian Restructuring: Challenges for the Rule of Law", in J. P. Sarra, ed., *Annual Review of Insolvency Law 2005* (2006), 481, at p. 481).

22 While insolvency proceedings may be governed by different statutory schemes, they share some commonalities. The most prominent of these is the single proceeding model. The nature and purpose of the single proceeding model are described by Professor Wood in *Bankruptcy and Insolvency Law*:

> They all provide a collective proceeding that supersedes the usual civil process available to creditors to enforce their claims. The creditors' remedies are collectivized in order to prevent the free-for-all that would otherwise prevail if creditors were permitted to exercise their remedies. In the absence of a collective process, each creditor is armed with the knowledge that if they do not strike hard and swift to seize the debtor's assets, they will be beat out by other creditors. [pp. 2-3]

The single proceeding model avoids the inefficiency and chaos that would attend insolvency if each creditor initiated proceedings to recover its debt. Grouping all possible actions against the debtor into a single proceeding controlled in a single forum facilitates negotiation with creditors because it places them all on an equal footing, rather than exposing them to the risk that a more aggressive creditor will realize its claims against the debtor's limited assets while the other creditors attempt a compromise. With a view to achieving that purpose, both the *CCAA* and the *BIA* allow a court to order all actions against a debtor to be stayed while a compromise is sought.

23 Another point of convergence of the *CCAA* and the *BIA* relates to priorities. Because the *CCAA* is silent

about what happens if reorganization fails, the *BIA* scheme of liquidation and distribution necessarily supplies the backdrop for what will happen if a *CCAA* reorganization is ultimately unsuccessful. In addition, one of the important features of legislative reform of both statutes since the enactment of the *BIA* in 1992 has been a cut-back in Crown priorities (S.C. 1992, c. 27, s. 39; S.C. 1997, c. 12, ss. 73 and 125; S.C. 2000, c. 30, s. 148; S.C. 2005, c. 47, ss. 69 and 131; S.C. 2009, c. 33, ss. 25 and 29; see also *Alternative granite & marbre inc., Re*, 2009 SCC 49, [2009] 3 S.C.R. 286, [2009] G.S.T.C. 154 (S.C.C.); *Quebec (Deputy Minister of Revenue) c. Rainville* (1979), [1980] 1 S.C.R. 35 (S.C.C.); *Proposed Bankruptcy Act Amendments: Report of the Advisory Committee on Bankruptcy and Insolvency* (1986)).

24 With parallel *CCAA* and *BIA* restructuring schemes now an accepted feature of the insolvency law landscape, the contemporary thrust of legislative reform has been towards harmonizing aspects of insolvency law common to the two statutory schemes to the extent possible and encouraging reorganization over liquidation (see *An Act to establish the Wage Earner Protection Program Act, to amend the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act and to make consequential amendments to other Acts*, S.C. 2005, c. 47; *Gauntlet Energy Corp., Re*, 2003 ABQB 894; [2003] G.S.T.C. 193, 30 Alta. L.R. (4th) 192 (Alta. Q.B.), at para. 19).

25 Mindful of the historical background of the *CCAA* and *BIA*, I now turn to the first question at issue.

3.2 GST Deemed Trust Under the CCAA

26 The Court of Appeal proceeded on the basis that the *ETA* precluded the court from staying the Crown's enforcement of the GST deemed trust when partially lifting the stay to allow the debtor to enter bankruptcy. In so doing, it adopted the reasoning in a line of cases culminating in *Ottawa Senators*, which held that an *ETA* deemed trust remains enforceable during *CCAA* reorganization despite language in the *CCAA* that suggests otherwise.

27 The Crown relies heavily on the decision of the Ontario Court of Appeal in *Ottawa Senators* and argues that the later in time provision of the *ETA* creating the GST deemed trust trumps the provision of the *CCAA* purporting to nullify most statutory deemed trusts. The Court of Appeal in this case accepted this reasoning but not all provincial courts follow it (see, e.g., *Komunik Corp., Re*, 2009 QCCS 6332 (Que. S.C.), leave to appeal granted, 2010 QCCA 183 (Que. C.A.)). Century Services relied, in its written submissions to this Court, on the argument that the court had authority under the *CCAA* to continue the stay against the Crown's claim for unremitted GST. In oral argument, the question of whether *Ottawa Senators* was correctly decided nonetheless arose. After the hearing, the parties were asked to make further written submissions on this point. As appears evident from the reasons of my colleague Abella J., this issue has become prominent before this Court. In those circumstances, this Court needs to determine the correctness of the reasoning in *Ottawa Senators*.

28 The policy backdrop to this question involves the Crown's priority as a creditor in insolvency situations which, as I mentioned above, has evolved considerably. Prior to the 1990s, Crown claims largely enjoyed priority in insolvency. This was widely seen as unsatisfactory as shown by both the 1970 and 1986 insolvency reform proposals, which recommended that Crown claims receive no preferential treatment. A closely related matter was whether the *CCAA* was binding at all upon the Crown. Amendments to the *CCAA* in 1997 confirmed that it did indeed bind the Crown (see *CCAA*, s. 21, as am. by S.C. 1997, c. 12, s. 126).

29 Claims of priority by the state in insolvency situations receive different treatment across jurisdictions worldwide. For example, in Germany and Australia, the state is given no priority at all, while the state enjoys

> (b) any provision of the *Canada Pension Plan* or of the *Employment Insurance Act* that refers to subsection 224(1.2) of the *Income Tax Act* and provides for the collection of a contribution ....

Therefore, not only does the *CCAA* provide that Crown claims do not enjoy priority over the claims of other creditors (s. 18.3(1)), but the exceptions to this rule (i.e., that Crown priority is maintained for source deductions) are repeatedly stated in the statute.

40 The apparent conflict in this case is whether the rule in the *CCAA* first enacted as s. 18.3 in 1997, which provides that subject to certain explicit exceptions, statutory deemed trusts are ineffective under the *CCAA*, is overridden by the one in the *ETA* enacted in 2000 stating that GST deemed trusts operate despite any enactment of Canada except the *BIA*. With respect for my colleague Fish J., I do not think the apparent conflict can be resolved by denying it and creating a rule requiring both a statutory provision enacting the deemed trust, and a second statutory provision confirming it. Such a rule is unknown to the law. Courts must recognize conflicts, apparent or real, and resolve them when possible.

41 A line of jurisprudence across Canada has resolved the apparent conflict in favour of the *ETA*, thereby maintaining GST deemed trusts under the *CCAA*. *Ottawa Senators*, the leading case, decided the matter by invoking the doctrine of implied repeal to hold that the later in time provision of the *ETA* should take precedence over the *CCAA* (see also *Solid Resources Ltd., Re* (2002), 40 C.B.R. (4th) 219, [2003] G.S.T.C. 21 (Alta. Q.B.); *Gauntlet*

42 The Ontario Court of Appeal in *Ottawa Senators* rested its conclusion on two considerations. First, it was persuaded that by explicitly mentioning the *BIA* in *ETA* s. 222(3), but not the *CCAA*, Parliament made a deliberate choice. In the words of MacPherson J.A.:

> The *BIA* and the *CCAA* are closely related federal statutes. I cannot conceive that Parliament would specifically identify the *BIA* as an exception, but accidentally fail to consider the *CCAA* as a possible second exception. In my view, the omission of the *CCAA* from s. 222(3) of the *ETA* was almost certainly a considered omission. [para. 43]

43 Second, the Ontario Court of Appeal compared the conflict between the *ETA* and the *CCAA* to that before this Court in *Doré c. Verdun (Municipalité)*, [1997] 2 S.C.R. 862 (S.C.C.), and found them to be "identical" (para. 46). It therefore considered *Doré* binding (para. 49). In *Doré*, a limitations provision in the more general and recently enacted *Civil Code of Québec*, S.Q. 1991, c. 64 ("*C.C.Q.*"), was held to have repealed a more specific provision of the earlier Quebec *Cities and Towns Act*, R.S.Q., c. C-19, with which it conflicted. By analogy, the Ontario Court of Appeal held that the later in time and more general provision, s. 222(3) of the *ETA*, impliedly repealed the more specific and earlier in time provision, s. 18.3(1) of the *CCAA* (paras. 47-49).

44 Viewing this issue in its entire context, several considerations lead me to conclude that neither the reasoning nor the result in *Ottawa Senators* can stand. While a conflict may exist at the level of the statutes' wording, a purposive and contextual analysis to determine Parliament's true intent yields the conclusion that Parliament could not have intended to restore the Crown's deemed trust priority in GST claims under the *CCAA* when it amended the *ETA* in 2000 with the *Sparrow Electric* amendment.

45 I begin by recalling that Parliament has shown its willingness to move away from asserting priority for Crown claims in insolvency law. Section 18.3(1) of the *CCAA* (subject to the s. 18.3(2) exceptions) provides that the Crown's deemed trusts have no effect under the *CCAA*. Where Parliament has sought to protect certain

Crown claims through statutory deemed trusts and intended that these deemed trusts continue in insolvency, it has legislated so explicitly and elaborately. For example, s. 18.3(2) of the *CCAA* and s. 67(3) of the *BIA* expressly provide that deemed trusts for source deductions remain effective in insolvency. Parliament has, therefore, clearly carved out exceptions from the general rule that deemed trusts are ineffective in insolvency. The *CCAA* and *BIA* are in harmony, preserving deemed trusts and asserting Crown priority only in respect of source deductions. Meanwhile, there is no express statutory basis for concluding that GST claims enjoy a preferred treatment under the *CCAA* or the *BIA*. Unlike source deductions, which are clearly and expressly dealt with under both these insolvency statutes, no such clear and express language exists in those Acts carving out an exception for GST claims.

46 The internal logic of the *CCAA* also militates against upholding the *ETA* deemed trust for GST. The *CCAA* imposes limits on a suspension by the court of the Crown's rights in respect of source deductions but does not mention the *ETA* (s. 11.4). Since source deductions deemed trusts are granted explicit protection under the *CCAA*, it would be inconsistent to afford a better protection to the *ETA* deemed trust absent explicit language in the *CCAA*. Thus, the logic of the *CCAA* appears to subject the *ETA* deemed trust to the waiver by Parliament of its priority (s. 18.4).

47 Moreover, a strange asymmetry would arise if the interpretation giving the *ETA* priority over the *CCAA* urged by the Crown is adopted here: the Crown would retain priority over GST claims during *CCAA* proceedings but not in bankruptcy. As courts have reflected, this can only encourage statute shopping by secured creditors in cases such as this one where the debtor's assets cannot satisfy both the secured creditors' and the Crown's claims (*Gauntlet*, at para. 21). If creditors' claims were better protected by liquidation under the *BIA*, creditors' incentives would lie overwhelmingly with avoiding proceedings under the *CCAA* and not risking a failed reorganization. Giving a key player in any insolvency such skewed incentives against reorganizing under the *CCAA* can only undermine that statute's remedial objectives and risk inviting the very social ills that it was enacted to avert.

48 Arguably, the effect of *Ottawa Senators* is mitigated if restructuring is attempted under the *BIA* instead of the *CCAA*, but it is not cured. If *Ottawa Senators* were to be followed, Crown priority over GST would differ depending on whether restructuring took place under the *CCAA* or the *BIA*. The anomaly of this result is made manifest by the fact that it would deprive companies of the option to restructure under the more flexible and responsive *CCAA* regime, which has been the statute of choice for complex reorganizations.

49 Evidence that Parliament intended different treatments for GST claims in reorganization and bankruptcy is scant, if it exists at all. Section 222(3) of the *ETA* was enacted as part of a wide-ranging budget implementation bill in 2000. The summary accompanying that bill does not indicate that Parliament intended to elevate Crown priority over GST claims under the *CCAA* to the same or a higher level than source deductions claims. Indeed, the summary for deemed trusts states only that amendments to existing provisions are aimed at "ensuring that employment insurance premiums and Canada Pension Plan contributions that are required to be remitted by an employer are fully recoverable by the Crown in the case of the bankruptcy of the employer" (Summary to S.C. 2000, c. 30, at p. 4a). The wording of GST deemed trusts resembles that of statutory deemed trusts for source deductions and incorporates the same overriding language and reference to the *BIA*. However, as noted above, Parliament's express intent is that only source deductions deemed trusts remain operative. An exception for the *BIA* in the statutory language establishing the source deductions deemed trusts accomplishes very little, because the explicit language of the *BIA* itself (and the *CCAA*) carves out these source deductions deemed trusts and maintains their effect. It is however noteworthy that no equivalent language maintaining GST deemed trusts

scribe the statutory override of deemed trusts. The comments cited by my colleague only emphasize the clear intent of Parliament to maintain its policy that only source deductions deemed trusts survive in *CCAA* proceedings.

55 In the case at bar, the legislative context informs the determination of Parliament's legislative intent and supports the conclusion that *ETA* s. 222(3) was not intended to narrow the scope of the *CCAA's* override provision. Viewed in its entire context, the conflict between the *ETA* and the *CCAA* is more apparent than real. I would therefore not follow the reasoning in *Ottawa Senators* and affirm that *CCAA* s. 18.3 remained effective.

56 My conclusion is reinforced by the purpose of the *CCAA* as part of Canadian remedial insolvency legislation. As this aspect is particularly relevant to the second issue, I will now discuss how courts have interpreted the scope of their discretionary powers in supervising a *CCAA* reorganization and how Parliament has largely endorsed this interpretation. Indeed, the interpretation courts have given to the *CCAA* helps in understanding how the *CCAA* grew to occupy such a prominent role in Canadian insolvency law.

3.3 Discretionary Power of a Court Supervising a CCAA Reorganization

57 Courts frequently observe that "[t]he *CCAA* is skeletal in nature" and does not "contain a comprehensive code that lays out all that is permitted or barred" (*ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.*, 2008 ONCA 587, 92 O.R. (3d) 513 (Ont. C.A.), at para. 44, *per* Blair J.A.). Accordingly, "[t]he history of CCAA law has been an evolution of judicial interpretation" (*Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Gen. Div. [Commercial List])), at para. 10, *per* Farley J.).

58 *CCAA* decisions are often based on discretionary grants of jurisdiction. The incremental exercise of judicial discretion in commercial courts under conditions one practitioner aptly describes as "the hothouse of real-time litigation" has been the primary method by which the *CCAA* has been adapted and has evolved to meet contemporary business and social needs (see Jones, at p. 484).

59 Judicial discretion must of course be exercised in furtherance of the *CCAA's* purposes. The remedial purpose I referred to in the historical overview of the Act is recognized over and over again in the jurisprudence. To cite one early example:

> The legislation is remedial in the purest sense in that it provides a means whereby the devastating social and economic effects of bankruptcy or creditor initiated termination of ongoing business operations can be avoided while a court-supervised attempt to reorganize the financial affairs of the debtor company is made.
>
> (*Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 41 O.A.C. 282 (Ont. C.A.), at para. 57, *per* Doherty J.A., dissenting)

60 Judicial decision making under the *CCAA* takes many forms. A court must first of all provide the conditions under which the debtor can attempt to reorganize. This can be achieved by staying enforcement actions by creditors to allow the debtor's business to continue, preserving the *status quo* while the debtor plans the compromise or arrangement to be presented to creditors, and supervising the process and advancing it to the point where it can be determined whether it will succeed (see, e.g., *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 51 B.C.L.R. (2d) 84 (B.C. C.A.), at pp. 88-89; *Pacific National Lease Holding Corp., Re* (1992), 19 B.C.A.C. 134 (B.C. C.A. [In Chambers]), at para. 27). In doing so, the court must often be cognizant of the various interests at stake in the reorganization, which can extend beyond those of the debtor and creditors to include

employees, directors, shareholders, and even other parties doing business with the insolvent company (see, e.g., *Canadian Airlines Corp., Re*, 2000 ABQB 442, 84 Alta. L.R. (3d) 9 (Alta. Q.B.), at para. 144, *per* Paperny J. (as she then was); *Air Canada, Re* (2003), 42 C.B.R. (4th) 173 (Ont. S.C.J. [Commercial List]), at para. 3; *Air Canada, Re* [2003 CarswellOnt 4967 (Ont. S.C.J. [Commercial List])], 2003 CanLII 49366, at para. 13, *per* Farley J.; Sarra, *Creditor Rights*, at pp. 181-92 and 217-26). In addition, courts must recognize that on occasion the broader public interest will be engaged by aspects of the reorganization and may be a factor against which the decision of whether to allow a particular action will be weighed (see, e.g., *Canadian Red Cross Society / Société Canadienne de la Croix Rouge, Re* (2000), 19 C.B.R. (4th) 158 (Ont. S.C.J.), at para. 2, *per* Blair J. (as he then was); Sarra, *Creditor Rights*, at pp. 195-214).

61 When large companies encounter difficulty, reorganizations become increasingly complex. *CCAA* courts have been called upon to innovate accordingly in exercising their jurisdiction beyond merely staying proceedings against the debtor to allow breathing room for reorganization. They have been asked to sanction measures for which there is no explicit authority in the *CCAA*. Without exhaustively cataloguing the various measures taken under the authority of the *CCAA*, it is useful to refer briefly to a few examples to illustrate the flexibility the statute affords supervising courts.

62 Perhaps the most creative use of *CCAA* authority has been the increasing willingness of courts to authorize post-filing security for debtor in possession financing or super-priority charges on the debtor's assets when necessary for the continuation of the debtor's business during the reorganization (see, e.g., *Skydome Corp., Re* (1998), 16 C.B.R. (4th) 118 (Ont. Gen. Div. [Commercial List]); *United Used Auto & Truck Parts Ltd., Re*, 2000 BCCA 146, 135 B.C.A.C. 96 (B.C. C.A.), aff'g (1999), 12 C.B.R. (4th) 144 (B.C. S.C. [In Chambers]); and generally, J. P. Sarra, *Rescue! The Companies' Creditors Arrangement Act* (2007), at pp. 93-115). The *CCAA* has also been used to release claims against third parties as part of approving a comprehensive plan of arrangement and compromise, even over the objections of some dissenting creditors (see Metcalfe & Mansfield). As well, the appointment of a Monitor to oversee the reorganization was originally a measure taken pursuant to the *CCAA's* supervisory authority; Parliament responded, making the mechanism mandatory by legislative amendment.

63 Judicial innovation during *CCAA* proceedings has not been without controversy. At least two questions it raises are directly relevant to the case at bar: (1) what are the sources of a court's authority during *CCAA* proceedings? (2) what are the limits of this authority?

64 The first question concerns the boundary between a court's statutory authority under the *CCAA* and a court's residual authority under its inherent and equitable jurisdiction when supervising a reorganization. In authorizing measures during *CCAA* proceedings, courts have on occasion purported to rely upon their equitable jurisdiction to advance the purposes of the Act or their inherent jurisdiction to fill gaps in the statute. Recent appellate decisions have counselled against purporting to rely on inherent jurisdiction, holding that the better view is that courts are in most cases simply construing the authority supplied by the *CCAA* itself (see, e.g., *Skeena Cellulose Inc., Re*, 2003 BCCA 344, 13 B.C.L.R. (4th) 236 (B.C. C.A.), at paras. 45-47, *per* Newbury J.A.; *Stelco Inc. (Re)* (2005), 75 O.R. (3d) 5 (Ont. C.A.), paras. 31-33, *per* Blair J.A.).

65 I agree with Justice Georgina R. Jackson and Professor Janis Sarra that the most appropriate approach is a hierarchical one in which courts rely first on an interpretation of the provisions of the *CCAA* text before turning to inherent or equitable jurisdiction to anchor measures taken in a *CCAA* proceeding (see G. R. Jackson and J. Sarra, "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters", in J. P. Sarra, ed., *Annual Review of Insolvency*

an appropriately purposive and liberal interpretation under which the order was permissible. The Crown submits that Tysoe J.A. correctly held that the mandatory language of the *ETA* gave the court no option but to permit enforcement of the GST deemed trust when lifting the *CCAA* stay to permit the debtor to make an assignment under the *BIA*. Whether the *ETA* has a mandatory effect in the context of a *CCAA* proceeding has already been discussed. I will now address the question of whether the order was authorized by the *CCAA*.

74 It is beyond dispute that the *CCAA* imposes no explicit temporal limitations upon proceedings commenced under the Act that would prohibit ordering a continuation of the stay of the Crown's GST claims while lifting the general stay of proceedings temporarily to allow the debtor to make an assignment in bankruptcy.

75 The question remains whether the order advanced the underlying purpose of the *CCAA*. The Court of Appeal held that it did not because the reorganization efforts had come to an end and the *CCAA* was accordingly spent. I disagree.

76 There is no doubt that had reorganization been commenced under the *BIA* instead of the *CCAA*, the Crown's deemed trust priority for the GST funds would have been lost. Similarly, the Crown does not dispute that under the scheme of distribution in bankruptcy under the *BIA*, the deemed trust for GST ceases to have effect. Thus, after reorganization under the *CCAA* failed, creditors would have had a strong incentive to seek immediate bankruptcy and distribution of the debtor's assets under the *BIA*. In order to conclude that the discretion does not extend to partially lifting the stay in order to allow for an assignment in bankruptcy, one would have to assume a gap between the *CCAA* and the *BIA* proceedings. Brenner C.J.S.C.'s order staying Crown enforcement of the GST claim ensured that creditors would not be disadvantaged by the attempted reorganization under the *CCAA*. The effect of his order was to blunt any impulse of creditors to interfere in an orderly liquidation. His order was thus in furtherance of the *CCAA's* objectives to the extent that it allowed a bridge between the *CCAA* and *BIA* proceedings. This interpretation of the tribunal's discretionary power is buttressed by s. 20 of the *CCAA*. That section provides that the *CCAA* "may be applied together with the provisions of any Act of Parliament... that authorizes or makes provision for the sanction of compromises or arrangements between a company and its shareholders or any class of them", such as the *BIA*. Section 20 clearly indicates the intention of Parliament for the *CCAA* to operate *in tandem* with other insolvency legislation, such as the *BIA*.

77 The *CCAA* creates conditions for preserving the *status quo* while attempts are made to find common ground amongst stakeholders for a reorganization that is fair to all. Because the alternative to reorganization is often bankruptcy, participants will measure the impact of a reorganization against the position they would enjoy in liquidation. In the case at bar, the order fostered a harmonious transition between reorganization and liquidation while meeting the objective of a single collective proceeding that is common to both statutes.

78 Tysoe J.A. therefore erred in my view by treating the *CCAA* and the *BIA* as distinct regimes subject to a temporal gap between the two, rather than as forming part of an integrated body of insolvency law. Parliament's decision to maintain two statutory schemes for reorganization, the *BIA* and the *CCAA*, reflects the reality that reorganizations of differing complexity require different legal mechanisms. By contrast, only one statutory scheme has been found to be needed to liquidate a bankrupt debtor's estate. The transition from the *CCAA* to the *BIA* may require the partial lifting of a stay of proceedings under the *CCAA* to allow commencement of the *BIA* proceedings. However, as Laskin J.A. for the Ontario Court of Appeal noted in a similar competition between secured creditors and the Ontario Superintendent of Financial Services seeking to enforce a deemed trust, "[t]he two statutes are related" and no "gap" exists between the two statutes which would allow the enforcement of property interests at the conclusion of *CCAA* proceedings that would be lost in bankruptcy *Ivaco Inc. (Re)*

(2006), 83 O.R. (3d) 108 (Ont. C.A.), at paras. 62-63).

79 The Crown's priority in claims pursuant to source deductions deemed trusts does not undermine this conclusion. Source deductions deemed trusts survive under both the *CCAA* and the *BIA*. Accordingly, creditors' incentives to prefer one Act over another will not be affected. While a court has a broad discretion to stay source deductions deemed trusts in the *CCAA* context, this discretion is nevertheless subject to specific limitations applicable only to source deductions deemed trusts (*CCAA*, s. 11.4). Thus, if *CCAA* reorganization fails (e.g., either the creditors or the court refuse a proposed reorganization), the Crown can immediately assert its claim in unremitted source deductions. But this should not be understood to affect a seamless transition into bankruptcy or create any "gap" between the *CCAA* and the *BIA* for the simple reason that, regardless of what statute the reorganization had been commenced under, creditors' claims in both instances would have been subject to the priority of the Crown's source deductions deemed trust.

80 Source deductions deemed trusts aside, the comprehensive and exhaustive mechanism under the *BIA* must control the distribution of the debtor's assets once liquidation is inevitable. Indeed, an orderly transition to liquidation is mandatory under the *BIA* where a proposal is rejected by creditors. The *CCAA* is silent on the transition into liquidation but the breadth of the court's discretion under the Act is sufficient to construct a bridge to liquidation under the *BIA*. The court must do so in a manner that does not subvert the scheme of distribution under the *BIA*. Transition to liquidation requires partially lifting the *CCAA* stay to commence proceedings under the *BIA*. This necessary partial lifting of the stay should not trigger a race to the courthouse in an effort to obtain priority unavailable under the *BIA*.

81 I therefore conclude that Brenner C.J.S.C. had the authority under the *CCAA* to lift the stay to allow entry into liquidation.

3.4 Express Trust

82 The last issue in this case is whether Brenner C.J.S.C. created an express trust in favour of the Crown when he ordered on April 29, 2008, that proceeds from the sale of LeRoy Trucking's assets equal to the amount of unremitted GST be held back in the Monitor's trust account until the results of the reorganization were known. Tysoe J.A. in the Court of Appeal concluded as an alternative ground for allowing the Crown's appeal that it was the beneficiary of an express trust. I disagree.

83 Creation of an express trust requires the presence of three certainties: intention, subject matter, and object. Express or "true trusts" arise from the acts and intentions of the settlor and are distinguishable from other trusts arising by operation of law (see D. W. M. Waters, M. R. Gillen and L. D. Smith, eds., *Waters' Law of Trusts in Canada* (3rd ed. 2005), at pp. 28-29 especially fn. 42).

84 Here, there is no certainty to the object (i.e. the beneficiary) inferrable from the court's order of April 29, 2008, sufficient to support an express trust.

85 At the time of the order, there was a dispute between Century Services and the Crown over part of the proceeds from the sale of the debtor's assets. The court's solution was to accept LeRoy Trucking's proposal to segregate those monies until that dispute could be resolved. Thus there was no certainty that the Crown would actually be the beneficiary, or object, of the trust.

86 The fact that the location chosen to segregate those monies was the Monitor's trust account has no inde-

TAB 2

2008 CarswellOnt 4811, 2008 ONCA 587, 45 C.B.R. (5th) 163, 47 B.L.R. (4th) 123, 296 D.L.R. (4th) 135, 240 O.A.C. 245, 92 O.R. (3d) 513

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2008 CarswellOnt 4811

ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.

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 AND ARRANGEMENT INVOLVING METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS II CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS III CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS V CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS XI CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS XII CORP., 4446372 CANADA INC. AND 6932819 CANADA INC., TRUSTEES OF THE CONDUITS LISTED IN SCHEDULE "A" HERETO

THE INVESTORS REPRESENTED ON THE PAN-CANADIAN INVESTORS COMMITTEE FOR THIRD-PARTY STRUCTURED ASSET-BACKED COMMERCIAL PAPER LISTED IN SCHEDULE "B" HERETO (Applicants / Respondents in Appeal) and METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS II CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS III CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS V CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS XI CORP., METCALFE & MANSFIELD ALTERNATIVE INVESTMENTS XII CORP., 4446372 CANADA INC. AND 6932819 CANADA INC., TRUSTEES OF THE CONDUITS LISTED IN SCHEDULE "A" HERETO (Respondents / Respondents in Appeal) and AIR TRANSAT A.T. INC., TRANSAT TOURS CANADA INC., THE JEAN COUTU GROUP (PJC) INC., AÉROPORTS DE MONTRÉAL INC., AÉROPORTS DE MONTRÉAL CAPITAL INC., POMERLEAU ONTARIO INC., POMERLEAU INC., LABOPHARM INC., DOMTAR INC., DOMTAR PULP AND PAPER PRODUCTS INC., GIRO INC., VÊTEMENTS DE SPORTS R.G.R. INC., 131519 CANADA INC., AIR JAZZ LP, PETRIFOND FOUNDATION COMPANY LIMITED, PETRIFOND FOUNDATION MIDWEST LIMITED, SERVICES HYPOTHÉCAIRES LA PATRIMONIALE INC., TECSYS INC. SOCIÉTÉ GÉNÉRALE DE FINANCEMENT DU QUÉBEC, VIBROSYSTM INC., INTERQUISA CANADA L.P., REDCORP VENTURES LTD., JURA ENERGY CORPORATION, IVANHOE MINES LTD., WEBTECH WIRELESS INC., WYNN CAPITAL CORPORATION INC., HY BLOOM INC., CARDACIAN MORTGAGE SERVICES, INC., WEST ENERGY LTD., SABRE ENERTY LTD., PETROLIFERA PETROLEUM LTD., VAQUERO RESOURCES LTD. and STANDARD ENERGY INC. (Respondents / Appellants)

Ontario Court of Appeal

J.I. Laskin, E.A. Cronk, R.A. Blair JJ.A.

Heard: June 25-26, 2008
Judgment: August 18, 2008[FN*]
Docket: CA C48969

Proceedings: affirming *ATB Financial v. Metcalfe & Mansfield Alternative Investments II Corp.* (2008), 2008

the powers of the court under it are not limitless. It is beyond controversy, however, that the CCAA is remedial legislation to be liberally construed in accordance with the modern purposive approach to statutory interpretation. It is designed to be a flexible instrument and it is that very flexibility which gives the Act its efficacy: *Canadian Red Cross Society / Société Canadienne de la Croix-Rouge, Re* (1998), 5 C.B.R. (4th) 299 (Ont. Gen. Div. [Commercial List]). As Farley J. noted in *Dylex Ltd., Re* (1995), 31 C.B.R. (3d) 106 (Ont. Gen. Div. [Commercial List]), at 111, "[t]he history of CCAA law has been an evolution of judicial interpretation."

45 Much has been said, however, about the "evolution of judicial interpretation" and there is some controversy over both the source and scope of that authority. Is the source of the court's authority statutory, discerned solely through application of the principles of statutory interpretation, for example? Or does it rest in the court's ability to "fill in the gaps" in legislation? Or in the court's inherent jurisdiction?

46 These issues have recently been canvassed by the Honourable Georgina R. Jackson and Dr. Janis Sarra in their publication "Selecting the Judicial Tool to get the Job Done: An Examination of Statutory Interpretation, Discretionary Power and Inherent Jurisdiction in Insolvency Matters,"[FN2] and there was considerable argument on these issues before the application judge and before us. While I generally agree with the authors' suggestion that the courts should adopt a hierarchical approach in their resort to these interpretive tools — statutory interpretation, gap-filling, discretion and inherent jurisdiction — it is not necessary in my view to go beyond the general principles of statutory interpretation to resolve the issues on this appeal. Because I am satisfied that it is implicit in the language of the CCAA itself that the court has authority to sanction plans incorporating third-party releases that are reasonably related to the proposed restructuring, there is no "gap-filling" to be done and no need to fall back on inherent jurisdiction. In this respect, I take a somewhat different approach than the application judge did.

47 The Supreme Court of Canada has affirmed generally — and in the insolvency context particularly — that remedial statutes are to be interpreted liberally and in accordance with Professor Driedger's modern principle of statutory interpretation. Driedger advocated that "the words of an Act are to be read in their entire context and in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament": *Rizzo & Rizzo Shoes Ltd., Re*, [1998] 1 S.C.R. 27 (S.C.C.) at para. 21, quoting E.A. Driedger, *Construction of Statutes*, 2nd ed. (Toronto: Butterworths, 1983); *Bell ExpressVu Ltd. Partnership v. Rex*, [2002] 2 S.C.R. 559 (S.C.C.) at para. 26.

48 More broadly, I believe that the proper approach to the judicial interpretation and application of statutes — particularly those like the CCAA that are skeletal in nature — is succinctly and accurately summarized by Jackson and Sarra in their recent article, *supra*, at p. 56:

> The exercise of a statutory authority requires the statute to be construed. The plain meaning or textualist approach has given way to a search for the object and goals of the statute and the intentionalist approach. This latter approach makes use of the purposive approach and the mischief rule, including its codification under interpretation statutes that every enactment is deemed remedial, and is to be given such fair, large and liberal construction and interpretation as best ensures the attainment of its objects. This latter approach advocates reading the statute as a whole and being mindful of Driedger's "one principle", that the words of the Act are to be read in their entire context, in their grammatical and ordinary sense harmoniously with the scheme of the Act, the object of the Act, and the intention of Parliament. It is important that courts first interpret the statute before them and exercise their authority pursuant to the statute, before reaching for other tools in the judicial toolbox. Statutory interpretation using the principles articulated above leaves room for gap-filling in the common law provinces and a consideration of purpose in *Québec* as a manifestation of the judge's overall task of statutory interpretation. Finally, the jurisprudence in relation to statutory interpretation demonstrates the fluidity inherent in the judge's task in seeking the objects of the statute and the intention of the legislature.

49 I adopt these principles.

50 The remedial purpose of the CCAA — as its title affirms — is to facilitate compromises or arrangements between an insolvent debtor company and its creditors. In *Hongkong Bank of Canada v. Chef Ready Foods Ltd.* (1990), 4 C.B.R. (3d) 311 (B.C. C.A.) at 318, Gibbs J.A. summarized very concisely the purpose, object and scheme of the Act:

> Almost inevitably, liquidation destroyed the shareholders' investment, yielded little by way of recovery to the creditors, and exacerbated the social evil of devastating levels of unemployment. The government of the day sought, through the C.C.A.A., to create a regime whereby the principals of the company and the creditors could be brought together under the supervision of the court to attempt a reorganization or compromise or arrangement under which the company could continue in business.

51 The CCAA was enacted in 1933 and was necessary — as the then Secretary of State noted in introducing the Bill on First Reading — "because of the prevailing commercial and industrial depression" and the need to alleviate the effects of business bankruptcies in that context: see the statement of the Hon. C.H. Cahan, Secretary of State, *House of Commons Debates (Hansard)* (April 20, 1933) at 4091. One of the greatest effects of that Depression was what Gibbs J.A. described as "the social evil of devastating levels of unemployment". Since then, courts have recognized that the Act has a broader dimension than simply the direct relations between the debtor company and its creditors and that this broader public dimension must be weighed in the balance together with the interests of those most directly affected: see, for example, *Nova Metal Products Inc. v. Comiskey (Trustee of)* (1990), 1 O.R. (3d) 289 (Ont. C.A.), *per* Doherty J.A. in dissent; *Skydome Corp., Re* (1998), 16 C.B.R. (4th) 125 (Ont. Gen. Div. [Commercial List]); *Anvil Range Mining Corp., Re* (1998), 7 C.B.R. (4th) 51 (Ont. Gen. Div. [Commercial List]).

52 In this respect, I agree with the following statement of Doherty J.A. in *Elan*, *supra*, at pp. 306-307:

> . . . [T]he Act was designed to serve a "broad constituency of investors, creditors and employees".[FN3] Because of that "broad constituency" the court must, when considering applications brought under the Act, *have regard not only to the individuals and organizations directly affected by the application, but also to the wider public interest.* [Emphasis added.]

Application of the Principles of Interpretation

53 An interpretation of the CCAA that recognizes its broader socio-economic purposes and objects is apt in this case. As the application judge pointed out, the restructuring underpins the financial viability of the Canadian ABCP market itself.

54 The appellants argue that the application judge erred in taking this approach and in treating the Plan and the proceedings as an attempt to restructure a financial market (the ABCP market) rather than simply the affairs between the debtor corporations who caused the ABCP Notes to be issued and their creditors. The Act is designed, they say, only to effect reorganizations between a corporate debtor and its creditors and not to attempt to restructure entire marketplaces.

55 This perspective is flawed in at least two respects, however, in my opinion. First, it reflects a view of the purpose and objects of the CCAA that is too narrow. Secondly, it overlooks the reality of the ABCP marketplace and the context of the restructuring in question here. It may be true that, in their capacity as ABCP *Dealers*, the releasee financial institutions are "third-parties" to the restructuring in the sense that they are not creditors of the debtor corporations. However, in their capacities as *Asset Providers* and *Liquidity Providers*, they are not only creditors but they are prior secured creditors to the Noteholders. Furthermore — as the application judge found — in these latter capacities they are making significant contributions to the restructuring by "foregoing immediate rights to assets and ... providing real and tangible input for the preservation and enhancement of the Notes" (para. 76). In this context,

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The Division of Powers and Paramountcy

102 Mr. Woods and Mr. Sternberg submit that extending the reach of the CCAA process to the compromise of claims as between solvent creditors of the debtor company and solvent third parties to the proceeding is constitutionally impermissible. They say that under the guise of the federal insolvency power pursuant to s. 91(21) of the *Constitution Act, 1867*, this approach would improperly affect the rights of civil claimants to assert their causes of action, a provincial matter falling within s. 92(13), and contravene the rules of public order pursuant to the *Civil Code of Quebec*.

103 I do not accept these submissions. It has long been established that the CCAA is valid federal legislation under the federal insolvency power: *Reference re Companies' Creditors Arrangement Act (Canada)*, [1934] S.C.R. 659 (S.C.C.). As the Supreme Court confirmed in that case (p. 661), citing Viscount Cave L.C. in *Quebec (Attorney General) v. Bélanger (Trustee of)*, [1928] A.C. 187 (Canada P.C.), "the exclusive legislative authority to deal with all matters within the domain of bankruptcy and insolvency is vested in Parliament." Chief Justice Duff elaborated:

> Matters normally constituting part of a bankruptcy scheme but not in their essence matters of bankruptcy and insolvency may, of course, from another point of view and in another aspect be dealt with by a provincial legislature; but, when treated as matters pertaining to bankruptcy and insolvency, they clearly fall within the legislative authority of the Dominion.

104 That is exactly the case here. The power to sanction a plan of compromise or arrangement that contains third-party releases of the type opposed by the appellants is embedded in the wording of the CCAA. The fact that this may interfere with a claimant's right to pursue a civil action — normally a matter of provincial concern — or trump Quebec rules of public order is constitutionally immaterial. The CCAA is a valid exercise of federal power. Provided the matter in question falls within the legislation directly or as necessarily incidental to the exercise of that power, the CCAA governs. To the extent that its provisions are inconsistent with provincial legislation, the federal legislation is paramount. Mr. Woods properly conceded this during argument.

Conclusion With Respect to Legal Authority

105 For all of the foregoing reasons, then, I conclude that the application judge had the jurisdiction and legal authority to sanction the Plan as put forward.

(2) The Plan is "Fair and Reasonable"

106 The second major attack on the application judge's decision is that he erred in finding that the Plan is "fair and reasonable" and in sanctioning it on that basis. This attack is centred on the nature of the third-party releases contemplated and, in particular, on the fact that they will permit the release of some claims based in fraud.

107 Whether a plan of compromise or arrangement is fair and reasonable is a matter of mixed fact and law, and one on which the application judge exercises a large measure of discretion. The standard of review on this issue is therefore one of deference. In the absence of a demonstrable error an appellate court will not interfere: see *Ravelston Corp., Re*, (2007), 31 C.B.R. (5th) 233 (Ont. C.A. [In Chambers]).

108 I would not interfere with the application judge's decision in this regard. While the notion of releases in favour of third parties — including leading Canadian financial institutions — that extend to claims of fraud is distasteful, there is no legal impediment to the inclusion of a release for claims based in fraud in a plan of compromise or arrangement. The application judge had been living with and supervising the ABCP restructuring from its outset. He was intimately attuned to its dynamics. In the end he concluded that the benefits of the Plan to the creditors as a whole, and to the debtor companies, outweighed the negative aspects of compelling the unwilling appellants to execute the re-

not constitute a new and hitherto untried "test" for the sanctioning of a plan under the CCAA. They simply represent findings of fact and inferences on the part of the application judge that underpin his conclusions on jurisdiction and fairness.

115 The appellants all contend that the obligation to release the third parties from claims in fraud, tort, breach of fiduciary duty, etc. is confiscatory and amounts to a requirement that they — as individual creditors — make the equivalent of a greater financial contribution to the Plan. In his usual lively fashion, Mr. Sternberg asked us the same rhetorical question he posed to the application judge. As he put it, how could the court countenance the compromise of what in the future might turn out to be fraud perpetrated at the highest levels of Canadian and foreign banks? Several appellants complain that the proposed Plan is unfair to them because they will make very little additional recovery if the Plan goes forward, but will be required to forfeit a cause of action against third-party financial institutions that may yield them significant recovery. Others protest that they are being treated unequally because they are ineligible for relief programs that Liquidity Providers such as Canaccord have made available to other smaller investors.

116 All of these arguments are persuasive to varying degrees when considered in isolation. The application judge did not have that luxury, however. He was required to consider the circumstances of the restructuring as a whole, including the reality that many of the financial institutions were not only acting as Dealers or brokers of the ABCP Notes (with the impugned releases relating to the financial institutions in these capacities, for the most part) but also as Asset and Liquidity Providers (with the financial institutions making significant contributions to the restructuring in these capacities).

117 In insolvency restructuring proceedings almost everyone loses something. To the extent that creditors are required to compromise their claims, it can always be proclaimed that their rights are being unfairly confiscated and that they are being called upon to make the equivalent of a further financial contribution to the compromise or arrangement. Judges have observed on a number of occasions that CCAA proceedings involve "a balancing of prejudices," inasmuch as everyone is adversely affected in some fashion.

118 Here, the debtor corporations being restructured represent the issuers of the more than $32 billion in non-bank sponsored ABCP Notes. The proposed compromise and arrangement affects that entire segment of the ABCP market and the financial markets as a whole. In that respect, the application judge was correct in adverting to the importance of the restructuring to the resolution of the ABCP liquidity crisis and to the need to restore confidence in the financial system in Canada. He was required to consider and balance the interests of *all* Noteholders, not just the interests of the appellants, whose notes represent only about 3% of that total. That is what he did.

119 The application judge noted at para. 126 that the Plan represented "a reasonable balance between benefit to all Noteholders and enhanced recovery for those who can make out specific claims in fraud" within the fraud carve-out provisions of the releases. He also recognized at para. 134 that:

> No Plan of this size and complexity could be expected to satisfy all affected by it. The size of the majority who have approved it is testament to its overall fairness. No plan to address a crisis of this magnitude can work perfect equity among all stakeholders.

120 In my view we ought not to interfere with his decision that the Plan is fair and reasonable in all the circumstances.

D. Disposition

121 For the foregoing reasons, I would grant leave to appeal from the decision of Justice Campbell, but dismiss the appeal.

TAB 3

2009 CarswellOnt 7383, 2009 ONCA 833, 77 C.C.P.B. 161, 59 C.B.R. (5th) 23, 2010 C.L.L.C. 210-005, 256 O.A.C. 131, 99 O.R. (3d) 708

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2009 CarswellOnt 7383, 2009 ONCA 833, 77 C.C.P.B. 161, 59 C.B.R. (5th) 23, 2010 C.L.L.C. 210-005, 256 O.A.C. 131, 99 O.R. (3d) 708

Nortel Networks Corp., Re

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

Donald Sproule, David D. Archibald and Michael Campbell on their own behalf and on behalf of Former Employees of Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation (Appellants) and Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation, the Board of Directors of Nortel Networks Corporation and Nortel Networks Limited, the Informal Nortel Noteholder Group, the Official Committee of Unsecured Creditors and Ernst & Young Inc. in its capacity as Monitor (Respondents)

National Automobile, Aerospace, Transportation and General Workers Union of Canada (CAW-Canada) and its Locals 27, 1525, 1530, 1535, 1837, 1839, 1905 and/or 1915, George Borosh and other retirees of Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation (Appellants) and Nortel Networks Corporation, Nortel Networks Limited, Nortel Networks Global Corporation, Nortel Networks International Corporation and Nortel Networks Technology Corporation, the Board of Directors of Nortel Networks Corporation and Nortel Networks Limited, the Informal Nortel Noteholder Group, the Official Committee of Unsecured Creditors and Ernst & Young Inc. in its capacity as Monitor (Respondents)

Ontario Court of Appeal

S.T. Goudge, K.N. Feldman, R.A. Blair JJ.A.

Heard: October 1, 2009
Judgment: November 26, 2009[FN*]
Docket: CA C50986, C50988

Proceedings: affirming *Nortel Networks Corp., Re* (2009), 2009 CarswellOnt 3583, 55 C.B.R. (5th) 68, 75 C.C.P.B. 233 (Ont. S.C.J. [Commercial List])

Counsel: Mark Zigler, Andrew Hatnay, Andrea McKinnon for Appellants, Nortel Networks Former Employees

40 The record before the court indicates that the motion judge made the initial order and the amended order in the context of the insolvency of a complex, multinational conglomerate as part of co-ordinated proceedings in a number of countries including the U.S. In June 2009, an Interim Funding and Settlement Agreement was negotiated which, together with the proceeds of certain ongoing asset sales, is providing funds necessary in the view of the court appointed Monitor, for the ongoing operations of Nortel during the next few months of the *CCAA* oversight operation. This funding was achieved on the basis that the stay applied to the severance and termination payments. The Monitor advises that if these payments were not subject to the stay and had to be funded, further financing would have to be found to do that and also maintain operations.

41 In that context, the motion judge exercised his discretion to impose a stay that could extend to the severance and termination payments. He considered the financial position of Nortel, that it was not carrying "business as usual" and that it was under financial pressure. He also considered that the *CCAA* proceeding is at an early stage, before the claims of creditor groups, including former employees and others have been considered or classified for ultimate treatment under a plan of arrangement. He noted that employees have no statutory priority and their claims are not secured claims.

42 While reference was made to the paramountcy doctrine by the motion judge, it was not the main focus of the argument before him. Nevertheless, he effectively concluded that it would thwart the intent of Parliament for the successful conduct of the *CCAA* restructuring if the initial order and the amended order could not include a stay provision that allowed Nortel to suspend the payment of statutory obligations for termination and severance under the *ESA*.

43 The respondents also argued that if the stay did not apply to statutory termination and severance obligations, then the employees who received these payments would in effect be receiving a "super-priority" over other unsecured or possibly even secured creditors on the assumption that in the end there will not be enough money to pay everyone in full. We agree that this may be the effect if the stay does not apply to these payments. However, that could also be the effect if Nortel chose to make such payments, as it is entitled to do under paragraph 6 (a) of the amended initial order. Of course, in that case, any such payments would be made in consultation with appropriate parties including the Monitor, resulting in the effective grant of a consensual rather than a mandatory priority. Even in this case, the motion judge provided a "hardship" alleviation program funded up to $750,000, to allow payments to former employees in clear need. This will have the effect of granting the "super-priority" to some. This is an acceptable result in appropriate circumstances.

44 However, this result does not in any way undermine the paramountcy analysis. That analysis is driven by the need to preserve the ability of the *CCAA* court to ensure, through the scope of the stay order, that Parliament's intent for the operation of the *CCAA* regime is not thwarted by the operation of provincial legislation. The court issuing the stay order considers all of the circumstances and can impose an order that has the effect of overriding a provincial enactment where it is necessary to do so.

45 Morawetz J. was satisfied that such a stay was necessary in the circumstances of this case. We see no error in that conclusion on the record before him and before this court.

46 Another issue was raised based on the facts of this restructuring as it has developed. It appears that the company will not be restructured, but instead its assets will be sold. It is necessary to continue operations in order to maintain maximum value for this process to achieve the highest prices and therefore the best outcome for all stakeholders. It is true that the basis for the very broad stay power has traditionally been expressed as a necessary aspect of the restructuring process, leading to a plan of arrangement for the newly restructured entity. However, we see no reason in the present circumstances why the same analysis cannot apply during a sale process that requires the business to be carried on as a going concern. No party has taken the position that the *CCAA* process is no longer available

because it is not proceeding as a restructuring, nor has any party taken steps to turn the proceeding into one under the *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3.

47 The former employee appellants have raised the constitutional question whether the doctrine of paramountcy applies to give to the *CCAA* judge the authority, under s. 11 of the Act, to order a stay of proceedings that has the effect of overriding s. 11(5) of the *ESA*, which requires almost immediate payment of termination and severance obligations. The answer to this question is yes.

48 We note again that the question before this court was limited to the effect of the stay on the timing of required statutory payments under the *ESA* and does not deal with the inter-relation of the *ESA* and the *CCAA* for the purposes of the plan of arrangement and the ultimate payment of these statutory obligations.

49 The appeal by the former employees is also dismissed.

***R.A. Blair J.A.*:**

I agree.

Appeals dismissed.

FN* A corrigendum issued by the court on December 8, 2009 has been incorporated herein.

FN1 The analogous section to the former s. 11.3(a) is now found in s. 11.01(a) of the recently amended *CCAA*.

FN2 The issue of post-initial order employee terminations, and specifically whether any portion of the termination or severance that may be owed is attributable to post-initial order services, was not at issue in this motion. In *Windsor Machine & Stamping Ltd., Re*, [2009] O.J. No. 3195 (Ont. S.C.J. [Commercial List]), decided one month after this motion, the issue was discussed more fully and Morawetz J. determined that it could be decided as part of a post-filing claim. Leave to appeal has been filed.

END OF DOCUMENT

TAB 4

Her Majesty The Queen in right of the Province of British Columbia *Appellant*

v.

Henfrey Samson Belair Ltd. *Respondent*

and

The Attorney General of Canada, the Attorney General for Ontario, the Attorney General of Quebec, the Attorney General of Nova Scotia, the Attorney General for New Brunswick, the Attorney General of Manitoba, the Attorney General for Alberta and the Attorney General of Newfoundland *Interveners*

INDEXED AS: BRITISH COLUMBIA *v.* HENFREY SAMSON BELAIR LTD.

File No.: 20515.

1989: April 21; 1989: July 13.

Present: Lamer, Wilson, La Forest, L'Heureux-Dubé, Gonthier, Cory and McLachlin JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Bankruptcy — Priority — Statutorily created trust for tax collected — Tax collected commingled with bankrupt's assets — All assets applied to reduce bank's indebtedness — Whether or not province should be given priority over other creditors because of statutorily created trust — Bankruptcy Act, R.S.C. 1970, c. B-3, ss. 47(a), 107(1)(j) — Social Service Tax Act, R.S.B.C. 1979, c. 388, s. 18.

Tops Pontiac Buick Ltd. collected provincial sales tax in the course of its business operations, as required by the *Social Service Tax Act*, and mingled the tax collected with its other assets. A creditor placed Tops in receivership and Tops then made an assignment in bankruptcy. The receiver sold the assets and applied the full proceeds to reduce the bank's indebtedness.

The province contended that the *Social Service Tax Act* created a statutory trust over the assets of Tops equal to the amount of the sales tax collected but not remitted, and that it had priority over the bank and all other creditors for this amount. The chambers judge

Sa Majesté La Reine du chef de la province de la Colombie-Britannique *Appelante*

c.

Henfrey Samson Belair Ltd. *Intimée*

et

Le procureur général du Canada, le procureur général de l'Ontario, le procureur général du Québec, le procureur général de la Nouvelle-Écosse, le procureur général du Nouveau-Brunswick, le procureur général du Manitoba, le procureur général de l'Alberta et le procureur général de Terre-Neuve *Intervenants*

RÉPERTORIÉ: COLOMBIE-BRITANNIQUE *c.* HENFREY SAMSON BELAIR LTD.

N° du greffe: 20515.

1989: 21 avril; 1989: 13 juillet.

Présents: Les juges Lamer, Wilson, La Forest, L'Heureux-Dubé, Gonthier, Cory et McLachlin.

EN APPEL DE LA COUR D'APPEL DE LA COLOMBIE-BRITANNIQUE

Faillite — Priorité — Fiducie créée par la Loi à l'égard des taxes perçues — Taxes perçues et confondues avec les biens de la faillie — Affectation de tous les biens de la faillie à la réduction de la créance de la Banque — La province doit-elle avoir priorité sur les autres créanciers en raison de la fiducie créée par la loi? — Loi sur la faillite, S.R.C. 1970, chap. B-3, art. 47a), 107(1)j) — Social Service Tax Act, R.S.B.C. 1979, chap. 388, art. 18.

La société Tops Pontiac Buick Ltd. a perçu la taxe provinciale de vente dans le cours de ses opérations commerciales, comme elle était tenue de le faire en vertu de la *Social Service Tax Act*, et elle a confondu les montants de taxe perçus avec ses autres biens. Un créancier de Tops l'a placée sous séquestre et Tops a alors déclaré faillite et fait cession de ses biens. Le séquestre a vendu les biens et consacré la totalité du produit de cette vente à la réduction de la créance de la Banque.

La province a soutenu que la *Social Service Tax Act* crée une fiducie sur les biens de Tops jusqu'à concurrence du montant de taxe de vente perçu mais non remis et qu'à l'égard de ce montant, elle a priorité sur la Banque et sur tous les autres créanciers. Le juge en

(d) the person required to collect or remit the tax under paragraph (b); or

(e) the estate of the person required to collect or remit the tax under paragraph (d).

The province argues that s. 18(1) creates a trust within s. 47(*a*) of the *Bankruptcy Act*, which provides:

47. The property of a bankrupt divisible among his creditors shall not comprise

(*a*) property held by the bankrupt in trust for any other person,

The respondent, on the other hand, submits that the deemed statutory trust created by s. 18 of the *Social Service Tax Act* is not a trust within s. 47 of the *Bankruptcy Act*, in that it does not possess the attributes of a true trust. It submits that the province's claim to the tax money is in fact a debt falling under s. 107(1)(*j*) of the *Bankruptcy Act*, the priority to which falls to be determined according to the priorities established by s. 107.

107. (1) Subject to the rights of secured creditors, the proceeds realized from the property of a bankrupt shall be applied in priority of payment as follows:

. . .

(*j*) claims of the Crown not previously mentioned in this section, in right of Canada or of any province, *pari passu* notwithstanding any statutory preference to the contrary.

Discussion

The issue may be characterized as follows. Section 47(*a*) of the *Bankruptcy Act* exempts trust property in the hands of the bankrupt from distribution to creditors, giving trust claimants absolute priority. Section 107(1) establishes priorities between creditors on distribution; s. 107(1)(*j*) ranks Crown claims last. Section 18 of the *Social Service Tax Act* creates a statutory trust which lacks the essential characteristics of a trust, namely, that the property impressed with the trust be identifiable or traceable. The question is whether the statutory trust created by the provincial legislation is a trust within s. 47(*a*) of the *Bankruptcy Act* or a mere Crown claim under s. 107(1)(*j*).

d) de la personne tenue de percevoir ou de remettre la taxe en vertu de l'alinéa b); ou

e) du patrimoine de la personne tenue de percevoir ou de remettre la taxe en vertu de l'alinéa d).

La province soutient que le par. 18(1) crée une fiducie au sens de l'al. 47*a*) de la *Loi sur la faillite*, dont voici le texte:

47. Les biens d'un failli, constituant le patrimoine attribué à ses créanciers, ne comprennent pas les biens suivants:

a) les biens détenus par le failli en fiducie pour toute autre personne,

De son côté, l'intimée fait valoir que la fiducie réputée créée par l'art. 18 de la *Social Service Tax Act* n'est pas une fiducie au sens de l'art. 47 de la *Loi sur la faillite*, en ce qu'elle n'a pas les attributs d'une véritable fiducie. L'intimée soutient que la réclamation du montant de la taxe par la province est en réalité une créance assujettie à l'al. 107(1)*j*) de la *Loi sur la faillite*, dont le rang est déterminé selon l'ordre de priorité établi à l'art. 107.

107. (1) Sous réserve des droits des créanciers garantis, les montants réalisés provenant des biens d'un failli doivent être distribués d'après l'ordre de priorité de paiement suivant:

. . .

j) les réclamations, non précédemment mentionnées au présent article, de la Couronne du chef du Canada ou d'une province du Canada, *pari passu*, nonobstant tout privilège statutaire à l'effet contraire.

Analyse

On peut formuler ainsi la question en litige: l'al. 47*a*) de la *Loi sur la faillite* soustrait, du patrimoine attribué aux créanciers, les biens détenus en fiducie par le failli et accorde la priorité absolue aux bénéficiaires de la fiducie. Le paragraphe 107(1) détermine le rang des différents créanciers pour les fins de la répartition; l'al. 107(1)*j*) place les créances de la Couronne au dernier rang. L'article 18 de la *Social Service Tax Act* établit une fiducie à laquelle il manque un des attributs essentiels de la fiducie, savoir un bien sujet à la fiducie qui puisse être identifié ou retracé. La question qui se pose est de savoir si la fiducie établie par la loi provinciale est une fiducie au sens de l'al. 47*a*) de la *Loi sur la faillite* ou une simple réclamation de la Couronne au sens de l'al. 107(1)*j*).

In my opinion, the answer to this question lies in the construction of the relevant provisions of the *Bankruptcy Act* and the *Social Service Tax Act*.

In approaching this task, I take as my guide the following passage from Driedger, *Construction of Statutes* (2nd ed. 1983), at p. 105:

> The decisions ... indicate that the provisions of an enactment relevant to a particular case are to be read in the following way:
>
> 1. The Act as a whole is to be read in its entire context so as to ascertain the intention of Parliament (the law as expressly or impliedly enacted by the words), the object of the Act (the ends sought to be achieved), and the scheme of the Act (the relation between the individual provisions of the Act).
>
> 2. The words of the individual provisions to be applied to the particular case under consideration are then to be read in their grammatical and ordinary sense in the light of the intention of Parliament embodied in the Act as a whole, the object of the Act and the scheme of the Act, and if they are clear and unambiguous and in harmony with that intention, object and scheme and with the general body of the law, that is the end.

With these principles in mind, I turn to the construction of ss. 47(*a*) and 107(1)(*j*) of the *Bankruptcy Act*. The question which arises under s. 47(*a*) of the Act concerns the meaning of the phrase "property held by the bankrupt in trust for any other person". Taking the words in their ordinary sense, they connote a situation where there is property which can be identified as being held in trust. That property is to be removed from other assets in the hands of the bankrupt before distribution under the *Bankruptcy Act* because, in equity, it belongs to another person. The intention of Parliament in enacting s. 47(*a*), then, was to permit removal of property which can be specifically identified as not belonging to the bankrupt under general principles of trust law from the distribution scheme established by the *Bankruptcy Act*.

Section 107(1)(*j*), on the other hand, has been held to deal not with rights conferred by general law, but with the statutorily created claims of federal and provincial tax collectors. The purpose of s. 107(1)(*j*) was discussed by this Court in *Deputy Minister of Revenue v. Rainville*, [1980] 1

Selon moi, la réponse à cette question dépend de l'interprétation des dispositions applicables de la *Loi sur la faillite* et de la *Social Service Tax Act*.

En m'attaquant à cette tâche, je m'inspire du passage suivant de l'ouvrage de Driedger intitulé *Construction of Statutes* (2e éd. 1983), à la p. 105:

> [TRADUCTION] La jurisprudence [...] indique qu'il faut interpréter ainsi les dispositions législatives pertinentes dans une affaire particulière:
>
> 1. Il faut interpréter l'ensemble de la Loi en fonction de tout son contexte pour déterminer l'intention du législateur (la Loi selon sa teneur expresse ou implicite), l'objet de la Loi (les fins qu'elle poursuit) et l'économie de la Loi (les liens entre les différentes dispositions de la Loi).
>
> 2. Il faut ensuite interpréter les termes des dispositions particulières applicables à l'affaire en cause selon leur sens grammatical et ordinaire, en fonction de l'intention du législateur manifestée dans l'ensemble de la Loi, de l'objet de la Loi et de l'économie de la Loi. S'ils sont clairs et précis, et conformes à l'intention, à l'objet, à l'économie et à l'ensemble de la Loi, l'analyse s'arrête là.

Gardant à l'esprit ces principes, j'aborde maintenant l'interprétation des al. 47*a*) et 107(1)*j*) de la *Loi sur la faillite*. L'alinéa 47*a*) de la Loi soulève la question du sens de l'expression «les biens détenus par le failli en fiducie pour toute autre personne». Selon leur sens ordinaire, ces mots renvoient à une situation où il existe des biens qui peuvent être identifiés comme étant détenus en fiducie. Ces biens doivent être retirés des autres biens que le failli détient avant leur répartition conformément à la *Loi sur la faillite* parce qu'en *equity* ils appartiennent à une autre personne. En adoptant l'al. 47*a*), le législateur a donc voulu permettre de soustraire, du régime de répartition établi par la *Loi sur la faillite*, les biens qui peuvent être spécifiquement identifiés comme n'appartenant pas au failli selon les principes généraux du droit des fiducies.

D'autre part, on a jugé que l'al. 107(1)*j*) porte non pas sur les droits conférés par le droit général, mais sur les créances établies par la loi en faveur du fisc fédéral et provincial. Cette Cour a déjà examiné l'objet de l'al. 107(1)*j*) dans l'arrêt *Sous-ministre du Revenu c. Rainville*, [1980] 1 R.C.S.

S.C.R. 35. Pigeon J., speaking for the majority, stated at p. 45:

> There is no need to consider the scope of the expression "claims of the Crown". It is quite clear that this applies to claims of provincial governments for taxes and I think it is obvious that it does not include claims not secured by Her Majesty's personal preference, but by a privilege which may be obtained by anyone under general rules of law, such as a vendor's or a builder's privilege.

If sections 47(*a*) and 107(1)(*j*) are read in this way, no conflict arises between them. If a trust claim is established under general principles of law, then the property subject to the trust is removed from the general distribution by reason of s. 47(*a*). Following the reasoning of Pigeon J. in *Deputy Minister of Revenue v. Rainville*, such a claim would not fall under s. 107(1)(*j*) because it is valid under general principles of law and is not a claim secured by the Crown's personal preference.

This construction of ss. 47(*a*) and 107(1)(*j*) of the *Bankruptcy Act* conforms with the principle that provinces cannot create priorities under the *Bankruptcy Act* by their own legislation, a principle affirmed by this Court in *Deloitte Haskins and Sells Ltd. v. Workers' Compensation Board*, [1985] 1 S.C.R. 785. As Wilson J. stated at p. 806:

> ... the issue in *Re Bourgault* [*Deputy Minister of Revenue v. Rainville*] and *Re Black Forest Restaurant Ltd.* was not whether a proprietary interest has been created under the relevant provincial legislation. It was whether provincial legislation, even if it did create a proprietary interest, could defeat the scheme of distribution under s. 107(1) of the *Bankruptcy Act*. These cases held that it could not, that while the provincial legislation could validly secure debts on the property of the debtor in a non-bankruptcy situation, once bankruptcy occurred s. 107(1) determined the status and priority of the claims specifically dealt with in the section. It was not open to the claimant in bankruptcy to say: By virtue of the applicable provincial legislation I am a secured creditor within the meaning of the opening words of s. 107(1) of the *Bankruptcy Act* and therefore the priority accorded my claim under the relevant paragraph of s. 107(1) does not apply to me. In effect, this is the position adopted by the Court of Appeal and advanced

35, où le juge Pigeon, s'exprimant au nom de la majorité, affirme à la p. 45:

> Il ne serait pas à propos de rechercher la portée exacte de l'expression «réclamations de la Couronne». Il est bien sûr qu'elle s'applique aux créances du fisc et il me paraît évident qu'elle ne saurait embrasser des créances garanties non par un privilège propre à Sa Majesté mais par un privilège dont toute autre personne peut jouir en vertu des principes généraux du droit tel que le privilège de vendeur, celui de constructeur, etc.

Interprétés de cette façon, les al. 47*a*) et 107(1)*j*) ne se contredisent pas. Si une réclamation fondée sur une fiducie est prouvée selon les principes généraux du droit, le bien sujet à la fiducie est soustrait à la répartition générale en raison de l'al. 47*a*). Selon le raisonnement du juge Pigeon dans l'arrêt *Sous-ministre du Revenu c. Rainville*, l'al. 107(1)*j*) ne s'appliquerait pas à une telle réclamation parce qu'elle est valide en vertu des principes généraux du droit et qu'elle ne constitue pas une créance garantie par un privilège propre à Sa Majesté.

Cette interprétation des al. 47*a*) et 107(1)*j*) de la *Loi sur la faillite* respecte le principe selon lequel les provinces ne peuvent, par leur propre loi, modifier l'ordre de priorité établi en vertu de la *Loi sur la faillite*. L'arrêt de cette Cour *Deloitte Haskins and Sells Ltd. c. Workers' Compensation Board*, [1985] 1 R.C.S. 785, a consacré ce principe. Comme l'affirme le juge Wilson, à la p. 806:

> ... dans les arrêts *Re Bourgault* [*Sous-ministre du Revenu c. Rainville*] et *Re Black Forest Restaurant Ltd.*, le litige n'était pas de savoir s'il y avait eu création d'un droit de propriété en vertu des lois provinciales applicables. Il s'agissait de savoir si, même si elle créait un droit de propriété, la loi provinciale pouvait aller à l'encontre du plan de distribution prévu au par. 107(1) de la *Loi sur la faillite*. Ces arrêts ont décidé qu'elle ne le pouvait pas et que, même si la loi provinciale pouvait validement créer une sûreté pour des dettes sur les biens du débiteur en dehors de la faillite, dès qu'il y avait faillite, le par. 107(1) déterminait le statut et la priorité des réclamations expressément mentionnées dans cet article. Il n'était pas loisible au créancier de la faillite de dire: en vertu de la loi provinciale applicable, je suis un créancier garanti au sens des premiers mots du par. 107(1) de la *Loi sur la faillite* et en conséquence la priorité que l'alinéa pertinent du par. 107(1) accorde à ma réclamation ne s'applique pas à moi. En réalité, c'est

before us by the respondent. It cannot be supported as a matter of statutory interpretation of s. 107(1) since, if the section were to be read in this way, it would have the effect of permitting the provinces to determine priorities on a bankruptcy, a matter within exclusive federal jurisdiction.

While *Deloitte Haskins and Sells Ltd. v. Workers' Compensation Board* was concerned with provincial legislation purporting to give the province the status of a secured creditor for purposes of the *Bankruptcy Act*, the same reasoning applies in the case at bar.

To interpret s. 47(*a*) as applying not only to trusts as defined by the general law, but to statutory trusts created by the provinces lacking the common law attributes of trusts, would be to permit the provinces to create their own priorities under the *Bankruptcy Act* and to invite a differential scheme of distribution on bankruptcy from province to province.

Practical policy considerations also recommend this interpretation of the *Bankruptcy Act*. The difficulties of extending s. 47(*a*) to cases where no specific property impressed with a trust can be identified are formidable and defy fairness and common sense. For example, if the claim for taxes equalled or exceeded the funds in the hands of the trustee in bankruptcy, the trustee would not recover the costs incurred to realize the funds. Indeed, the trustee might be in breach of the Act by expending funds to realize the bankrupt's assets. Other difficulties would arise in the case of more than one claimant to the trust property. The spectre is raised of a person who has a valid trust claim under the general principles of trust law to a specific piece of property, finding himself in competition with the Crown claiming a statutory trust in that and all the other property. Could the Crown's general claim pre-empt the property interest of the claimant under trust law? Or would the claimant under trust law prevail? To admit of such a possibility would be to run counter to the clear intention of Parliament, in enacting the *Bankruptcy Act*, of setting up a clear and orderly

la position adoptée par la Cour d'appel et plaidée devant nous par l'intimée. Cette position n'est pas étayée par l'interprétation législative du par. 107(1) puisque, si on interprétait l'article dans ce sens, il aurait pour effet de permettre aux provinces de déterminer les priorités en cas de faillite, ce qui relève de la compétence fédérale exclusive.

Bien que l'arrêt *Deloitte Haskins and Sells Ltd. c. Workers' Compensation Board* ait porté sur une disposition législative provinciale qui avait pour objet de conférer à la province le statut de créancier garanti pour les fins de la *Loi sur la faillite*, le même raisonnement vaut pour l'espèce.

Interpréter l'al. 47*a*) comme s'appliquant non seulement aux fiducies établies en vertu du droit général, mais aussi aux fiducies légales établies par les provinces, qui ne possèdent pas les attributs des fiducies de *common law*, reviendrait à permettre aux provinces d'établir leur propre ordre de priorité applicable à la *Loi sur la faillite* et à ouvrir la porte à l'établissement de régimes de répartition en cas de faillite différents d'une province à l'autre.

Des considérations pratiques générales favorisent aussi cette interprétation de la *Loi sur la faillite*. Les difficultés que peut susciter l'application de l'al. 47*a*) aux cas où il n'est pas possible d'identifier un bien précis sujet à une fiducie sont considérables et contraires à l'équité et au bon sens. Par exemple, si les créances pour taxes sont égales ou supérieures aux sommes que détient le syndic de faillite, ce dernier sera dans l'impossibilité de se faire indemniser des frais engagés pour réaliser l'actif. Le syndic pourrait même contrevenir à la Loi en engageant des dépenses pour réaliser l'actif du failli. La présence de plus d'un créancier à l'égard du bien en fiducie soulèverait d'autres difficultés. Imaginons le cas de la personne qui aurait une réclamation fondée sur une fiducie, valide selon les principes généraux du droit, à l'égard d'un bien précis et qui se trouverait en concurrence avec Sa Majesté qui invoquerait l'existence d'une fiducie légale concernant ce même bien et tous les autres biens. La créance générale de Sa Majesté pourrait-elle avoir priorité sur le droit de propriété du créancier en vertu du droit des fiducies? Ou encore, le créancier en vertu

scheme for the distribution of the bankrupt's assets.

In summary, I am of the view that s. 47(*a*) should be confined to trusts arising under general principles of law, while s. 107(1)(*j*) should be confined to claims such as tax claims not established by general law but secured "by her Majesty's personal preference" through legislation. This conclusion, in my opinion, is supported by the wording of the sections in question, by the jurisprudence of this Court, and by the policy considerations to which I have alluded.

I turn next to s. 18 of the *Social Service Tax Act* and the nature of the legal interests created by it. At the moment of collection of the tax, there is a deemed statutory trust. At that moment the trust property is identifiable and the trust meets the requirements for a trust under the principles of trust law. The difficulty in this, as in most cases, is that the trust property soon ceases to be identifiable. The tax money is mingled with other money in the hands of the merchant and converted to other property so that it cannot be traced. At this point it is no longer a trust under general principles of law. In an attempt to meet this problem, s. 18(1)(*b*) states that tax collected shall be deemed to be held separate from and form no part of the collector's money, assets or estate. But, as the presence of the deeming provision tacitly acknowledges, the reality is that after conversion the statutory trust bears little resemblance to a true trust. There is no property which can be regarded as being impressed with a trust. Because of this, s. 18(2) goes on to provide that the unpaid tax forms a lien and charge on the entire assets of the collector, an interest in the nature of a secured debt.

Applying these observations on s. 18 of the *Social Service Tax Act* to the construction of ss. 47(*a*) and 107(1)(*j*) of the *Bankruptcy Act* which

du droit des fiducies aurait-il priorité? Reconnaître l'existence d'une telle possibilité irait à l'encontre de l'intention clairement exprimée par le législateur, en adoptant la *Loi sur la faillite*, d'établir un régime clair et ordonné de répartition de l'actif d'un failli.

En résumé, j'estime que l'application de l'al. 47*a*) devrait se limiter aux fiducies établies en vertu des principes généraux du droit, alors que l'al. 107(1)*j*) devrait s'appliquer aux seules créances pour taxes qui ne découlent pas du droit général, mais qui sont garanties «par un privilège propre à Sa Majesté» par voie législative. À mon avis, le texte des dispositions en cause, la jurisprudence de cette Cour et les considérations de principe auxquelles j'ai fait allusion appuient cette conclusion.

J'examinerai maintenant l'art. 18 de la *Social Service Tax Act* et la nature des droits qu'il crée. Au moment de la perception de la taxe, il y a fiducie légale réputée. À ce moment-là, le bien en fiducie est identifiable et la fiducie répond aux exigences d'une fiducie établie en vertu des principes généraux du droit. La difficulté que présente l'espèce, qui est la même que dans la plupart des autres cas, vient de ce que le bien en fiducie cesse bientôt d'être identifiable. Le montant de la taxe est confondu avec d'autres sommes que détient le marchand et immédiatement affecté à l'acquisition d'autres biens de sorte qu'il est impossible de le retracer. Dès lors, il n'existe plus de fiducie de *common law*. Pour obvier à ce problème, l'al. 18(1)*b*) prévoit que la taxe perçue sera réputée être détenue de manière séparée et distincte des deniers, de l'actif ou du patrimoine de celui qui l'a perçue. Mais, comme l'existence de la disposition déterminative le reconnaît tacitement, en réalité, après l'affectation de la somme, la fiducie légale ressemble peu à une fiducie véritable. Il n'y a pas de bien qu'on puisse considérer comme sujet à la fiducie. Aussi, pour cette raison, le par. 18(2) ajoute que la taxe impayée emporte un privilège sur la totalité des biens de celui qui l'a perçue, c'est-à-dire un droit tenant d'une créance garantie.

Si j'applique ces observations relatives à l'art. 18 de la *Social Service Tax Act* à l'interprétation des al. 47*a*) et 107(1)*j*) de la *Loi sur la faillite* que j'ai

TAB 5

2006 CarswellOnt 6292, [2006] W.D.F.L. 3681, 56 C.C.P.B. 1, 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 26 B.L.R. (4th) 43

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Ivaco Inc., Re

IN THE MATTER OF the Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36.

AND IN THE MATTER OF A Plan or Plans of Compromise or Arrangement of Ivaco Inc. and the Applicants listed in Schedule "A"

Ontario Court of Appeal

J. Laskin, M. Rosenberg, J. Simmons JJ.A.

Heard: February 22, 2006
Judgment: October 17, 2006
Docket: CA C44455

Proceedings: affirming *Ivaco Inc., Re* (2005), 2005 CarswellOnt 3445, 47 C.C.P.B. 62, 12 C.B.R. (5th) 213 (Ont. S.C.J. [Commercial List])

Counsel: Frederick L. Myers, Jason Wadden for Appellant, Superintendent of Finance Services (Ontario)

Andrew Hatnay for Respondent, Quebec Pension Committee of Ivaco Inc.

Jeffrey S. Leon, Richard B. Swan for Respondent, National Bank of Canada

Dan V. MacDonald for Respondent, Bank of Nova Scotia

Geoff R. Hall for Respondent, QIT-Fer et Titane Inc.

Robert W. Staley, Evangelia Kriaris for Respondent, Informal Committee of Noteholders

Peter F.C. Howard for Monitor, Ernst & Young Inc.

Subject: Insolvency; Estates and Trusts; Family; Property; Corporate and Commercial; Civil Practice and Procedure

Bankruptcy and insolvency --- Property of bankrupt — Trust property — General principles

Pension funds — I Inc. and related companies, collectively I Group, had established various registered pension plans

(Receiver of) (1998), 39 O.R. (3d) 176 (Ont. C.A.). The second and third issues, I assume, will be dealt with at the hearing of the bankruptcy petitions. Admittedly, the motions judge made some observations on these two issues. However, he also said, at para. 20 of his reasons, that he was not deciding either one:

> However, in the circumstances, I do not find it appropriate to allow (indeed direct) that there be an assignment in bankruptcy on a "voluntary basis" as there is the s. 43(7) issue to be determined. Similarly with respect to the balance of declarations requested by the National Bank, while I have made some general observations as to reversing priorities, it would not be appropriate to determine with finality the priorities of various claims on the record before me at this time.

35 In their written and oral submissions, the Superintendent and the QPC argued that some of the motions judge's general observations on these issues were wrong. I do not propose to consider these arguments because, as the motions judge recognized, they should be addressed at the hearing of the bankruptcy petitions. Instead, I will make a few brief observations of my own.

36 In my view, the motions judge appropriately considered what would likely happen at the bankruptcy hearing. He did so because the likely implications of lifting the stay were relevant considerations to the exercise of his discretion.

37 The motions judge observed, at para. 14, that the discretion to refuse to make a bankruptcy order under s. 43(7) typically is exercised in two categories of cases: where the petitioner has an ulterior motive in seeking the order, or where the order would not serve any meaningful purpose. This observation reflects the current state of the case law under s. 43(7). See for example *Dallas/North Group Inc., Re* (1999), 46 O.R. (3d) 602 (Ont. Gen. Div.); *Lambert, Re* (2002), 60 O.R. (3d) 787 (Ont. C.A.). Although the motions judge added that the Superintendent's claim does not appear to come within either category, he left the final determination of that question for the bankruptcy judge.

38 The motions judge also observed, at para. 11 of his reasons, that a provincially created deemed trust does not by that fact alone enjoy priority under the BIA. This is not a contentious proposition. In a series of cases, the Supreme Court of Canada has repeatedly said that a province cannot, by legislating a deemed trust, alter the scheme of priorities under the federal statute. See for example *British Columbia v. Henfrey Samson Belair Ltd.*, [1989] 2 S.C.R. 24 (S.C.C.); *Husky Oil Operations Ltd. v. Minister of National Revenue*, [1995] 3 S.C.R. 453 (S.C.C.). Indeed, it is this jurisprudence that undoubtedly prompted the Superintendent's original motion and appeal to this court.

39 The motions judge also correctly observed, at para. 11 of his reasons, that a provincial deemed trust will retained its priority in bankruptcy only if it also meets the three attributes — the three certainties — of a common law trust: certainty of intent; certainty of subject matter; and certainty of object. Only a trust that has these three attributes is a "true trust" that will be exempt from the bankrupt's estate under s. 67(1)(a) of the BIA. See for example *Henfrey Sampson*, *supra*. Whether the Superintendent can establish a true trust for unpaid past service contributions, even though the proceeds of the Heico sale have been commingled, will be decided at the bankruptcy hearing.

40 I now turn to the issues that do arise on this appeal.

c) Did the motions judge err in law in failing to order immediate payment of the amount of the deemed trusts or in failing to segregate this amount?

41 The Superintendent's principal submission is that the motions judge erred in law in failing to order payment of the amount of the deemed trusts before bankruptcy or in failing to order the Monitor to segregate this amount during the CCAA proceedings. The submission that the motions judge was legally required to order payment or segregation of the amount of the deemed trusts was not advanced before him. The Superintendent advanced this submission for the first time in this court. I do not agree with it.

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42 I will deal first with whether the motions judge should have required the Monitor, Ernst & Young, to segregate the amount of the deemed trusts. The Superintendent contends that the Companies, and in their place the Monitor, had a statutory and fiduciary obligation to segregate. As the Monitor was an officer of the court, the motions judge should have compelled it to fulfill these duties. This contention faces three obstacles: the language of the PBA; the terms of the pension stay order; and the status and role of the Monitor.

43 The deemed trusts for unpaid past service and special contributions are found in ss. 57(3) and (4) of the PBA. Subsection (3) is the basic provision that creates a deemed trust for unpaid employer contributions. Subsection (4) stipulates that on the wind up of a pension plan, employer contributions accrued but not yet due because of the timing of the wind up are also deemed to be held in trust:

> s. 57(3) An employer who is required to pay contributions to a pension fund shall be deemed to hold in trust for the beneficiaries of the pension plan an amount of money equal to the employer contributions due and not paid into the pension fund.
>
> s. 57(4) Where a pension plan is wound up in whole or in part, an employer who is required to pay contributions to the pension fund shall be deemed to hold in trust for the beneficiaries of the pension plan an amount of money equal to employer contributions accrued to the date of the wind up but not yet due under the plan or regulations.

44 At para. 11 of his decision, the motions judge said that both unpaid contributions and wind-up liabilities are deemed to be held in trust under s. 57(3). In his earlier decision in *Toronto Dominion Bank v. Usarco Ltd.* (1991), 42 E.T.R. 235 (Ont. Gen. Div.), Farley J. said, at para. 25, that the equivalent legislation then in force under the *Pension Benefits Act, 1987*, S.O. 1987, c.35 referred only to unpaid contributions, not to wind-up liabilities. I think that the statement in *Usarco Ltd.* is correct, but I do not need to resolve the issue on this appeal.

45 Under s. 57(5) of the PBA the plan administrator has a lien and charge on the assets of the employer for the amount of any deemed trust. The lien and charge permit the administrator to enforce the deemed trust.

> s. 57(5) The administrator of the pension plan has a lien and charge on the assets of the employer in an amount equal to the amounts deemed to be held in trust under subsections (1), (3) and (4).

46 The Superintendent argues that these provisions required the Companies, and in their place the Monitor, to keep the unpaid contributions in a separate account. However, the language of s. 57 does not require the employer to hold the contributions separately. A "deemed trust" is, in a sense, a legal fiction. Outside of bankruptcy it does create a priority for pension contributions, a priority that would not exist but for the designation. Yet, as I have already said, this legislative designation by itself does not create a true trust. If the province wants to require an employer to keep its unpaid contributions to a pension plan in a separate account it must legislate that separation. It has not done so.

47 The Superintendent argues that the pension stay order supports her position because para. 5 the order, *supra*, recognized that a deemed trust for unpaid contributions may arise during the stay period and that para. 6 of the stay order, *supra*, did not compromise the Companies' obligation to make these contributions. This argument fails to take account of para. 4 of the pension stay order. Paragraph 4 stipulates that during the stay the Companies will not incur any obligation — statutory, fiduciary or otherwise — for failing to make contributions to the plan. In my view, the Superintendent's argument amounts to an impermissible collateral attack on para. 4 of the pension stay order.

48 The Superintendent also tries to buttress her position by arguing that the Monitor stands in the shoes of the Companies, and like the Companies, has a fiduciary duty to the pension beneficiaries. I disagree.

49 The Monitor was appointed under s. 11.7(1) of the CCAA to "monitor the business and financial affairs" of the

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Companies, and was given the functions set out in s. 11.7(3) of that statute: to examine the Companies' property, report to the court on the Companies' business and financial affairs and keep the creditors informed. Although the motions judge gave the Monitor additional powers, they were limited. The Monitor was given authority to deal with day-to-day administrative matters, to finalize the sale to Heico and to receive and control the proceeds of sale. I do not think it can be fairly said that the Monitor "stands in the shoes of the Companies".

50 Equally important, the Monitor does not owe a fiduciary duty to the pension beneficiaries. The Superintendent's attempt to impose an obligation on the Monitor to segregate the contributions to the non-union plans depends at least on establishing that the Monitor acts as a fiduciary of the employees in those plans. Both the role of the Monitor and the initial stay order preclude the Superintendent's assertion.

51 Pension plan administrators do owe a fiduciary duty to plan members. See E.E. Gillese, *The Fiduciary Liability of the Employer as Pension Plan Administrator* (Toronto: The Canadian Institute, November 18, 1996, pp. 1-25). But the Monitor was not given that role. It is not an administrator of any of the four non-union plans. Indeed, the Superintendent never asked the court to give the Monitor responsibility for administering these plans.

52 Moreover, para. 59 of the initial stay order expressly states that the Monitor is not to be considered either a successor or related employer.

> THIS COURT ORDERS that nothing in this Order shall result in the Monitor being or being deemed or considered to be a successor or related employer, sponsor or payor with respect to any Applicant or any employees or former employees of any Applicant under any legislation, including ... the *Pension Benefits Act* (Ontario) ... or under any other provincial or federal legislation, regulation or rule of law or equity applicable to employees or pensions, or otherwise.
>
> [Emphasis added].

As the Monitor was neither a plan administrator nor a successor employer, it can owe no fiduciary duty to the members of the four plans.

53 Therefore, the combination of the wording of s. 57 of the PBA, para. 4 of the pension stay order and the limited role of the Monitor, refute the Superintendent's segregation argument. The Superintendent, however, submits that two cases, the decision of this court in *GMAC Commercial Credit Corp. - Canada v. TCT Logistics Inc.* (2005), 74 O.R. (3d) 382 (Ont. C.A.) [hereinafter *TCT Logistics*] and an earlier decision of the motions judge in *Usarco Ltd.*, *supra*, support the argument for segregation. In my view, both cases are distinguishable.

54 In *TCT Logistics*, this court held that an interim receiver, who was both an officer of the court and stood in the shoes of the debtor, had a statutory duty under the legislation then in force, s. 15 of the *Load Brokers Regulation*, O.Reg. 556/92 (passed under the *Truck Transportation Act*, R.S.O. 1990, c. T.-22) to hold carriers' fees that it had collected in a separate trust account. *TCT Logistics* and this case differ in three critical ways.

55 First, the interim receiver in *TCT Logistics*, was not just an officer of the court, it stood in the place of the debtor company. Here, although the Monitor is an officer of the court, it does not stand in the place of the Companies. For the reasons outlined in para. 49 its role is far more limited.

56 Second, in *TCT Logistics* the court order authorized the interim receiver to hold the carriers' fees in a separate bank account until entitlement to that money was decided. Here, the pension stay order prohibited the Companies from making any past service or special contributions during the stay period.

57 Third, and perhaps most important, the applicable legislation in *TCT Logistics*, s. 15(2) of the *Load Brokers*

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Regulation required the debtor company to maintain a separate trust account and to keep the fees it collected for the carriers in that account. Here, s. 57 of the PBA does not similarly require an employer to keep its unpaid contributions in a separate trust account. Moreover, in *TCT Logistics*, despite s. 15(2) of the Regulation, this court held that the carrier fees previously collected by the debtor company lost their character as trust money because they had been commingled with other funds. *TCT Logistics* thus does not support the Superintendent's position.

58 In *Usarco Ltd.*, *supra*, at para. 16, Farley J. commented that the deemed trust provisions of the PBA "implied a fiduciary obligation on the part of Usarco", and that "a trustee in bankruptcy stepping into the shoes of Usarco must deal with that fiduciary obligation". These comments do not apply to this case. The Monitor here, unlike the trustee in bankruptcy in *Usarco Ltd.*, did not step into the shoes of the debtor. Thus, *Usarco Ltd.* does not assist the Superintendent.

59 For these reasons, I reject the Superintendent's argument that the motions judge was required in law to order the segregation of the amount of the deemed trusts during the CCAA proceeding. I now turn to the Superintendent's other submission: that the motions judge was required in law to order that the amount of the deemed trust be paid at the end of the CCAA proceedings, but before bankruptcy.

60 The CCAA itself did not require the motions judge to execute the deemed trusts. The Superintendent cannot point to any section of the statute where a legal obligation to order payment of the past service contributions can be found. Moreover, in my view, absent an agreement, I doubt that the CCAA even authorized the motions judge to order this payment. Once restructuring was not possible and the CCAA proceedings were spent, as the motions judge found and all parties acknowledged, I question whether the court had any authority to order a distribution of the sale proceeds. See for example *United Maritime Fishermen Co-op., Re* (1988), 68 C.B.R. (N.S.) 170 (N.B. Q.B.), at 173.

61 The Superintendent's submission that the motions judge was required to order payment of the outstanding contributions rests on the proposition that a gap exists between the CCAA and the BIA in which the provincial deemed trusts can be executed. This proposition runs contrary to the federal bankruptcy and insolvency regime and to the principle that the province cannot reorder priorities in bankruptcy.

62 The federal insolvency regime includes the CCAA and the BIA. The two statutes are related. A debtor company under the CCAA is defined in s. 2 by the company's bankruptcy or insolvency. Section 11(3) authorizes a thirty-day stay of any current or prospective proceedings under the BIA, and s. 11(4) authorizes an extension of the initial thirty-day period. During the stay period, creditor claims and bankruptcy proceedings are suspended. Once the stay is lifted by court order or terminates by its own terms, simultaneously the creditor claims and bankruptcy proceedings are revived and may go forward.

63 For the Superintendent's position to be correct, there would have to be a gap between the end of the CCAA period and bankruptcy proceedings, in which the pension beneficiaries' rights under the deemed trusts crystallize before the rights of all other creditors, including their right to bring a bankruptcy petition. That position is illogical. All rights must crystallize simultaneously at the end of the CCAA period. There is simply no gap in the federal insolvency regime in which the provincial deemed trusts alone can operate. That is obviously so on the facts in this case because the Bank of Nova Scotia had already commenced a petition for bankruptcy, which was stayed by the initial order under the CCAA. Once the motions judge lifted the stay, the petition was revived. In my view, however, the situation would be the same even if no bankruptcy petition was pending.

64 Where a creditor seeks to petition a debtor company into bankruptcy at the end of CCAA proceedings, any claim under a provincial deemed trust must be dealt with in bankruptcy proceedings. The CCAA and the BIA create a complementary and interrelated scheme for dealing with the property of insolvent companies, a scheme that occupies the field and ousts the application of provincial legislation. Were it otherwise, creditors might be tempted to forgo efforts to restructure a debtor company and instead put the company immediately into bankruptcy. That would not be

2006 CarswellOnt 6292, [2006] W.D.F.L. 3681, 56 C.C.P.B. 1, 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 26 B.L.R. (4th) 43

a desirable result.

65 Also, giving effect to the Superintendent's position, in substance, would allow a province to do indirectly what it is precluded from doing directly. Just as a province cannot directly create its own priorities or alter the scheme of distribution of property under the BIA, neither can it do so indirectly. See *Husky Oil, supra*, at paras. 32 and 39. At bottom the Superintendent seeks to alter the scheme for distributing an insolvent company's assets under the BIA. It cannot do so.

66 The Superintendent relies on one authority in support of its position: the decision of the motions judge in *Usarco Ltd., supra*. In that case, although a bankruptcy petition had been brought, Farley J. nonetheless ordered the receiver to pay to the pension plan administrator the amount of the deemed trusts under the PBA. However, the facts in *Usarco Ltd.* differed materially from the facts in this case.

67 In *Usarco Ltd.*, CCAA proceedings did not precede the bankruptcy petition. Moreover, in *Usarco Ltd.* the petitioning creditor was not proceeding with its bankruptcy petition because its principal had died, and no other creditor took steps to advance the petition. Thus, unlike in this case, in *Usarco Ltd.* it was unclear whether bankruptcy proceedings would ever take place.

68 Recently in *General Chemical Canada Ltd., Re* (Ont. S.C.J.), Campbell J. relied on this distinction, followed the motions judge's decision in the present case and refused to order payment of the amount of the deemed trusts under the PBA. He wrote at para. 35:

> To conclude otherwise (absent improper motive on the part of Company or a major creditor) would be to negate both CCAA proceedings and bankruptcy proceedings by preventing creditors from pursuing a process of equitable distribution of the debtor's property as they believe it to be when making their decisions.

I agree. The factual differences between *General Chemical Canada Ltd.* and this case on the one hand, and *Usarco Ltd.* on the other, render *Usarco Ltd.* of no assistance to the Superintendent on this appeal.

69 Because the federal legislative regime under the CCAA and the BIA determines the claims of creditors of an insolvent company, if the rights of pension claimants are to be given greater priority, Parliament, not the courts, must do so. And Parliament has at least signalled its intention to do so. Last year it passed the *Wage Earner Protection Program Act*, S.C. 2005 c.47. That Act would amend the BIA and give special priority to unpaid pension contributions of a bankrupt employer. This statute, however, has not been proclaimed in force. That it was passed perhaps shows that under the existing legislative regime, claims like that of the Superintendent must fail. I would reject this ground of appeal.

d) Did the motions judge err in the exercise of his discretion by lifting the stay and permitting the bankruptcy petitions to proceed?

70 In my view, the motions judge's order lifting the stay was a discretionary order. He summarized his reasons for rejecting the Superintendent's position and exercising his discretion to allow the bankruptcy petitions to proceed at para. 18 of his decision:

> In the end result I do not see that the Superintendent has made a compelling case to the effect that the petitions in bankruptcy should not be allowed to proceed in the ordinary course. I have reached that conclusion by weighing the factors pro and con as discussed above, including the relative benefits to all stakeholders (including workers and pensioners) to maintaining the CCAA proceedings (with the benefit of the suspension of past contributions as per the unopposed and un-reconsidered order of November 28, 2003), the fact that no reorganization is now possible as all Ivaco Companies (except Docap) have ceased operations and are without operational assets and

2007 CarswellOnt 2855, 370 N.R. 395 (note), 238 O.A.C. 400 (note)

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2007 CarswellOnt 2855, 370 N.R. 395 (note), 238 O.A.C. 400 (note)

Ivaco Inc., Re

Superintendent of Financial Services v. National Bank of Canada, Informal Committee of Noteholders and Ernst & Young Inc., in it's capacity as Court-Appointed Monitor, Qit-Fer et Titane Inc. and Bank of Nova Scotia

Supreme Court of Canada

Bastarache J., Fish J., LeBel J.

Judgment: May 3, 2007
Docket: 31761

Proceedings: Leave to appeal allowed, 2006 C.E.B. & P.G.R. 8218, 25 C.B.R. (5th) 176, 83 O.R. (3d) 108, 275 D.L.R. (4th) 132, 2006 CarswellOnt 6292, 56 C.C.P.B. 1, [2006] W.D.F.L. 3681 (Ont. C.A.); Affirmed, 2005 CarswellOnt 3445, [2005] O.J. No. 3337, 47 C.C.P.B. 62, 12 C.B.R. (5th) 213, [2005] W.D.F.L. 3789 (Ont. S.C.J. [Commercial List])

Counsel: None given

Subject: Insolvency; Estates and Trusts; Family; Property; Corporate and Commercial; Civil Practice and Procedure

Bankruptcy and insolvency.

Pensions.

Per Curiam:

1 The application for leave to appeal from the judgment of the Court of Appeal for Ontario, Number C44455, dated October 17, 2006, is granted with costs to the applicant in any event of the cause.

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TAB 6

Report of the Expert Commission on Pensions

A Fine Balance

Safe Pensions
Affordable Plans
Fair Rules

Report of the Expert Commission on Pensions

A Fine Balance

Safe Pensions
Affordable Plans
Fair Rules

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COMMISSION D'EXPERTS EN REGIMES DE RETRAITE

October 31, 2008

Hon. Dwight Duncan
Minister of Finance for Ontario

Dear Minister Duncan,

I have the honour to present to you *A Fine Balance*, the report of the Ontario Expert Commission on Pensions.

While as Commissioner I remain solely responsible for the text of the report and its recommendations, these are the work of many hands — those of my public-spirited as well as expert Advisors, of my hard-working and capable staff and, not least, of the many Ontarians who communicated their hopes and concerns, and contributed their knowledge and views, to the Commission over the past two years. In addition, the Commission's work was greatly assisted by research studies undertaken for it by Canadian and international pension experts, by the information provided by the Financial Services Commission of Ontario and by the logistical support provided by the Ministry of Finance.

I thank the many individuals, organizations and agencies referred to above for their willingness to address frankly, intelligently and constructively the difficult issues of pension policy, law and administration that fell within my mandate. And I thank you, Mr. Minister — and your predecessor, the Hon. Greg Sorbara — for the opportunity to serve as Commissioner.

The aspiration to strike the right balance — a fine balance — among safe pensions, affordable plans and fair rules is widely shared across the pension community and beyond. I wish you and your officials every success in working with all interested parties to find such a balance and to translate it into a new pension regime for Ontario.

Sincerely,

H.W. Arthurs
Commissioner

addition, I recommend in Chapter Seven that both the Superintendent and the new Pension Tribunal of Ontario (PTO) should be provided with plenary powers to remedy all violations of the PBA and the regulations. Thus, it should now be possible to put into operation the principle of graduated regulatory responses outlined in Chapter One.

However, effective regulation depends not simply on having powers, but also on using them and being seen to do so. At the moment, the Superintendent relies heavily on informal strategies to deal with delinquent sponsors that have failed to pay their contributions, relatively rarely on prosecution, and seldom on other legal enforcement strategies. While this informal approach does achieve the desired results in most cases, it has two shortcomings. First, those who have violated the PBA and, in some cases, imperilled a pension plan, end up simply doing what they ought to have done in the first place — at no additional cost to themselves, except, perhaps, having to pay interest on overdue remittances. Second, informal disposition does not generate a demonstration effect that might deter other potential wrongdoers. While I certainly do not favour the gratuitous use of remedial or punitive powers, I do think that the regulator ought to adopt a more comprehensive and proactive approach to compliance. The integrity of individual plans, and of the system as a whole, depends if not on total compliance, then as near to it as practicable.

> Recommendation 6-6 — The regulator should create an office of compliance to deal with the failure of sponsors to remit contributions and other violations of the *Pension Benefits Act* that imperil the security of pension plans and impede regulatory oversight of the pension system. That office should also maintain, for its own purposes and for the benefit of interested parties, an on-line register of delinquent sponsors and other offenders, and the measures taken to deal with them.

None of the recommendations in this section deals directly with a situation where the sponsor of a SEPP is insolvent or bankrupt. Such situations must, of course, be dealt with under federal bankruptcy and insolvency statutes, which, however, do not apply to pension plans *per se*. In the next section of this chapter, I address the interface between these federal statutes and provincial pension law.

6.3 Fair Treatment of Pension Plans and Beneficiaries in the Event of Sponsor Bankruptcy or Insolvency

6.3.1 Introduction

As I indicated in Chapter One, an important principle shaping this report is the desirability of better coordination among public policies that affect the pension system. The disjuncture between provincial pension law and federal bankruptcy and insolvency law is a prime example of the need for improved coordination.

6.3.2 The protection of pension funds under federal insolvency legislation

Under the federal *Companies' Creditors Arrangement Act* (CCAA), companies with debts greater than $5 million are permitted to seek court protection — in effect, a temporary suspension of their obligation to pay their debts — pending approval of a restructuring plan by creditors and/or the supervising court. Restructuring typically involves permanent forgiveness by creditors of some or all of the debt. Arrears of pension plan contributions are treated like any other debt. But while future accruals may be dealt with in the CCAA process, the reduction of accrued benefits may not. That said, active plan members may be willing to surrender some of their rights in order to retain their jobs and keep the company afloat and the plan in force.

If the CCAA process succeeds, the corporation's debt is restructured; it is discharged from court protection; and it remains a going concern. In these circumstances, it will pay its pension contribution arrears according to regulatory requirements and its other debts under whatever terms are agreed upon or ordered. Moreover, its obligation to pay future contributions will be revived on the original basis, unless the plan has been cancelled by the sponsor, or a reduction in its future terms has been consented to by the active and retired members (usually under pressure) or ordered by the court.

If a company does not qualify for CCAA proceedings, or if those proceedings do not result in successful restructuring, the federal *Bankruptcy and Insolvency Act* (BIA) comes into play. The BIA also permits restructuring, but if this fails, the insolvent firm is wound up and its assets are distributed among its creditors. Secured creditors must be paid in full before unsecured creditors are eligible to receive payment. If insufficient funds are available to pay them in full, unsecured creditors are paid on a *pro rata* basis. Crucially, debts owed to a pension fund have up to now been classed as unsecured and therefore, as a practical matter, have often been unrecoverable. However, the new federal *Wage Earner Protection Program Act* — recently proclaimed in force — will accord pension funds a degree of protection somewhat more consistent with their importance under provincial legislation. Under this new legislation, the "normal cost" of plans — that is, arrears of current contributions as defined by federal regulations — is to be accorded priority over other claims under the BIA, although unfunded liabilities and solvency deficiencies are not.

While it improves the position of pension plans, their active members and retirees, this legislation does not fully respond to arguments made by some in favour of giving higher preference to pension claims in bankruptcy and insolvency proceedings.

The extent to which pension plans and their active and retired members ought to be protected against the consequences of sponsor insolvency is a matter of considerable debate. On the one hand, while employees trade current wages for the promise of future pension income, they may not understand that this arrangement entails the risk that the sponsor may become insolvent or bankrupt. On the other, employees in given circumstances may indeed understand the risk but tacitly or explicitly accept it in order to keep the sponsor in business and avoid cancellation of the plan. Moreover, giving pension liabilities a higher priority in restructuring and insolvency proceedings would likely create private market pressures for better funding of pension plans. While no bad thing in itself, however, this pressure might have a detrimental effect on the employer's ability to raise capital, stay in business, provide jobs and fund the pension plan; indeed, it might result in lenders and investors more aggressively resisting the establishment or maintenance of pension plans, even if insolvency is not immediately a prospect.

The debate raises complex issues, most of which, however, must ultimately be resolved by federal, not provincial, legislators.

> **Recommendation 6-7** — The government of Ontario should support recent federal legislation that gives priority to unpaid current pension service costs in the event of bankruptcy. It should also initiate discussions with the federal government concerning the possibility of extending similar priority to all special payments to fund both solvency deficiencies and unfunded liabilities owing to the plan by the sponsor at the time of insolvency.

The recent federal legislation also provides that in the event an arrangement involving the priority claims of a pension plan is reached with the insolvent's creditors, any change in the priority for current service costs will be approved by a court only if the Superintendent has approved the arrangement.

> **Recommendation 6-8** — The *Pension Benefits Act* should be amended to permit the Superintendent to approve arrangements and changes in arrangements that involve the claims of pension plans under federal bankruptcy legislation.

One submission to the Commission from a law firm that represents active and retired plan members proposed that Ontario could take steps under provincial law to treat all unpaid contributions as subject to a trust in favour of the plan and its beneficiaries. Indeed, the PBA deems current contributions to be held in trust for the fund, and subjects the sponsor's assets to a lien and charge in favour of the plan administrator until payment is actually made. In principle, these provisions — or some revised version of them — might be construed as excluding those assets from the sponsor's estate and making them unavailable to other creditors in insolvency proceedings. However, provisions of the BIA appear to nullify or take precedence over the PBA provisions. Quite apart from the merits, unless and until this apparent constitutional impasse is resolved, it would be futile for me to recommend further changes to the PBA that are designed to create trusts or liens to withdraw unpaid contributions from the sponsor's estate, and to provide pension plans with enhanced protection in the event of bankruptcy or insolvency. While I am therefore not prepared to make a formal recommendation concerning this issue, I do urge that this question be studied by the province's law officers.

Finally, even though the province cannot alter the priorities established by federal law among creditors of the insolvent sponsor's estate, there is no reason why it cannot determine how a depleted pension plan apportions losses among its active and retired members. Current PBA regulations require *pro rata* distribution of the assets of the pension fund in these circumstances. For example, if a plan is 75% funded, then all active members and retirees receive 75% of their promised benefit, whatever it might be. However, it may be that different priorities would encourage more vigilant behaviour on the part of those who are in a position to detect or forestall the sponsor's insolvency, or to protect groups that are particularly vulnerable. For example, in the United Kingdom, retirees' claims are given priority over those of active members, perhaps on the ground that the latter were in a position to negotiate plan changes that may have affected the funded ratio. Plans might also be allowed to establish priorities specific to their own circumstances, although there is a risk that this might disadvantage retirees and others excluded from plan governance. Or, a third approach: recent benefit improvements could be excluded from payment in the event the plan has to be wound up while in deficiency, as they are under the PBGF. This latter approach was supported in several submissions to the Commission, and seems sensible to me.

Recommendation 6-9 — Plan assets should be distributed on a pro rata basis. However, benefit improvements introduced within the last five years should be postponed until after other benefits are paid, in accordance with Recommendation 6-5, above.

6.3.3 The representation of pension interests in federal bankruptcy and insolvency proceedings

What priority ought to be given pension funds in the event of the sponsor's insolvency or bankruptcy raises some difficult issues of public policy; whether the interests of pension funds and those of their beneficiaries should be entitled to effective representation in insolvency or bankruptcy proceedings does not. Clearly, as a matter of basic justice, all interested parties ought to have the right to be heard in any contentious proceedings. However, that right does not now clearly exist, and will not exist until certain modest changes have been made to federal bankruptcy legislation.

The task of protecting pension rights and interests might be assigned to the pension regulator; to the pension fund itself, acting through its administrator; or to the plan beneficiaries acting individually or collectively. However, the status of all three in bankruptcy and insolvency proceedings is unclear.

The pension regulator — the Superintendent — is arguably best placed to defend the interests of the pension fund against the other creditors of an insolvent sponsor. The Superintendent knows, or should know, more about the fund's claims than anyone else except the administrator, who is often compromised as being the *alter ego* of the sponsor responsible for deficiencies. The Superintendent also knows more about pension law and the pension system than any other potential litigant, and in defending the fund would be defending the system as well. The Superintendent's authoritative participation on behalf of the plan may reduce or eliminate the possibility that other parties — active and retired members and their representative organizations — will have to intervene on its behalf. And finally, the Superintendent has — or will have, if my recommendations are accepted — the legal and other resources necessary to negotiate and, if needs be, litigate on behalf of the fund. However, only when the Superintendent is subrogated to the rights of a sponsor whose plan members will be compensated by the PBGF, or when concessions under the regulatory regime are sought, does the Superintendent presently have an unchallenged right to appear in insolvency and bankruptcy proceedings.

Recommendation 6-10 — The Ontario government should seek to persuade the federal government to amend its bankruptcy and insolvency legislation to give the pension regulator the right to intervene in proceedings under that legislation to defend the interests of any pension fund and its members. Provincial law should allow the pension regulator to act on behalf of, and to assert all the rights and powers of, the plan administrator in the context of bankruptcy and insolvency proceedings, if the regulator believes such action is warranted.

If these changes in federal legislation can be negotiated, the pension regulator's role in proactively defending both pension plans and the PBGF would be reinforced. However, in order to take on these enlarged responsibilities in insolvency-related proceedings, the regulator would have to develop new capacities — the subject of recommendations elsewhere in this report — and to deploy staff dedicated to dealing with potential and actual sponsor insolvencies.

TAB 7

1991 CarswellOnt 540, 42 E.T.R. 235

1991 CarswellOnt 540, 42 E.T.R. 235

Toronto Dominion Bank v. Usarco Ltd.

Re USARCO LIMITED PENSION PLAN FOR ITS HOURLY EMPLOYEES; TORONTO-DOMINION BANK v. USARCO LIMITED and FRANK LEVY

Ontario Court of Justice (General Division)

Farley J.

Heard: June 4 and 17, 1991
Judgment: August 2, 1991
Docket: Doc. 52384/90

Counsel: *Harry Underwood*, for administrator.

M. MacNaughton, for Toronto-Dominion Bank.

N. Saxe, for receivers.

Subject: Estates and Trusts; Corporate and Commercial; Property; Insolvency

Bankruptcy --- Property of bankrupt — Trust property — General.

Pensions --- Surplus funds — Bankruptcy of employer.

Bankruptcy — Property of bankrupt — Trust property — Interaction of Bankruptcy Act and Pension Benefits Act, 1987 — Bankruptcy petition filed but not proceeded with — Claims of administrator of pension plan of bankrupt company having priority over claims of trustee in bankruptcy — Bankruptcy Act, R.S.C. 1985, c. B-3 — Pension Benefits Act, 1987, S.O. 1987, c. 35.

Pensions — Interaction of Pension Benefits Act, 1987 and Bankruptcy Act — Bankruptcy petition filed but not proceeded with — Claims of administrator of pension plan of bankrupt company having priority over claims of trustee in bankruptcy — Bankruptcy Act, R.S.C. 1985, c. B-3 — Pension Benefits Act, 1987, S.O. 1987, c. 35.

Pensions — Deemed trust under s. 58 of Pension Benefits Act, 1987 — Employer company wound up — Deemed trust to include moneys accrued but not yet due from employer to plan, and interest payable by employer on unpaid amounts — Pension Benefits Act, 1987, S.O. 1987, c. 35, ss. 58(4), 59(2).

on the part of Usarco. A trustee in bankruptcy stepping into the shoes of Usarco must deal with that fiduciary obligation.

17 It seems to me that the administrator's position would be stronger than the types of claims set out in the above cases since it comprises a trust claim. If so, then according to s. 67(*a*) of the *BA*, such trust property would not be property of a bankrupt divisible amongst its creditors. The administrator asserts that the deemed trust under the *PBA* has been converted into a true trust either (a) by notice or (b) by virtue of an actual separation of the funds by the receiver. A true trust would, if it exists, prevail against a competing claim of a trustee in bankruptcy. While it appears to me that the administrator gave notice to the receiver by the November and December letters (with an estimated amount of the deemed trust of $489,928), it does not seem that the receiver had notice of any further claim until June19, 1991 when the administrator advanced a further claim for approximately $600,000 plus interest. As to the question of an actual separation of funds by the receiver, the administrator relies on the terms of the undertaking given on one of the multiple adjournments of this matter. Its text is as follows:

> On consent adjourned to May 13, 1991 on the undertaking of the Receiver to
>
> 1. hold $500,000 collected since November 7, 1991 [sic] from the proceeds of accounts receivable and inventories at Usarco until the return of the motion on May 13, 1991, and
>
> 2. notify the Applicant of any motion for an order directing the Receiver to pay any funds in its hand to any creditor of Usarco or Frank Levy.

18

> (Indicated signed by counsel for the bank, receiver, and administrator.)

19 I would think that the claim of an actual separation of funds may not overreach what was said in this understanding. While there is no promise to hold the funds apart and separate per se, I do think that this can be inferred by the fact that para. 2 of the undertaking requires the receiver to notify the administrator of a motion to the effect of directing the receiver to pay out any funds (which I assume would include the $500,000 to any creditor of Usarco). The undertaking therefore would seem to have the $500,000 as being the subject matter of this judicial determination as to the administrator's trust claim. On this basis, it may meet the test of separation enunciated in the *Re I.B.L.* case, supra. Certainly, the administrator has given Usarco and the receiver notice, to the extent of $489,928.

20 If the funds are true trust funds, then they will not be property of Usarco in the event that Usarco is determined to be bankrupt (see s.67(*a*), *BA*). It is clear that if the funds are merely deemed to be trust funds, then such deeming is not sufficient to segregate such for the purposes of the *BA* (see: *Re I.B.L.* case, supra, at pp. 143-144 [O.R.]).

21 Section 58(4) of the *PBA* provides that the amount deemed to be held in trust on a wind-up situation is:

> equal to employer contributions accrued to the date of the wind-up but not yet due under the plan or regulations.

This should be contrasted with the language of s. 58(3), which deals with a non wind-up situation:

> equal to the employer contributions due and not paid into the pension fund.

Section 76(1)(*a*) obliges the employer in a wind-up situation to pay into the pension fund an amount "equal to the total of all payments that, under this Act, the regulations and the pension plan, are due or that have accrued and that have not been paid into the pension fund." In this context what do "accrued", "due", "not yet due", and "not yet paid" mean? What is the extent of the trust? Does it apply to the non-current and unfunded liability; does it support a claim for inter est?

22 The administrator relies on the analysis of Duff J. in *Ontario Hydro-Electric Power Commission v. Albright* (1922), 64 S.C.R. 306, [1923] 2 D.L.R. 578, to support its claim for the additional moneys, which are referred to as the non-current, unfunded liability. DuffJ. indicated at pp. 312-313 [S.C.R.]:

> The subjects of this provision are such interest and sums payable for the purpose of a sinking fund as shall have accrued but shall not be due at the time mentioned; and in order to apply the provision you must ascertain what interest and what sums of the character mentioned fall at the specified time within the described category — the category defined by the words
>
> > interest and sinking fund payments ... accrued ... but not yet due.
>
> The word 'due' in relation to moneys in respect of which there is a legal obligation to pay them may mean either that the facts making the obligation operative have come into existence with the exception that the day of payment has not yet arrived, or it may mean that the obligation has not only been completely constituted but is also presently exigible. That it is used in the latter sense, in the present instance is perfectly clear — otherwise the contrast expressed between payments 'accrued' and payments 'due' would, especially in the case of interest, be patent nonsense. The most natural meaning of such a phrase as 'accrued payments' would be, and standing alone it would *prima facie* receive that reading, moneys presently payable; but the word 'accrued' according to well recognized usage has, as applied to rights or liabilities the meaning simply of completely constituted — and it may have this meaning although it appears from the context that the right completely constituted or the liability completely constituted is one which is only exercisable or enforceable *in futuro* — a debt for example which is *debitum in praesenti solvendum in futuro*. It is in this sense that it has been widely applied to express the fact that such a liability has been created in relation to a sum of money, part of a whole (made up of an accumulation of such parts) which is not to be payable until a later date, and it is in this sense that it seems to be used in the clause before us.

23 Quite clearly, in a wind-up situation, the wording of s. 58(4) [*PBA*] is to oblige the employer (Usarco) with a trust arrangement concerning those contributions which are accrued, even though such may not be due under the plan. This is distinct from an ongoing situation envisaged by s. 58(3) [*PBA*], where such obligation is with respect to contributions which are then due but not yet paid over to the pension fund. Section 58(5) [*PBA*] gives the administrator a lien and a charge over the deemed trust amounts. By s. 58(6) [*PBA*], the deemed trust applies whether or not the employer kept these moneys separate and apart. It is clear from s. 76(1)(*a*) [*PBA*] that "due" and "accrued" are not identical, as they are referred to separately therein.

24 The Regulations to the *PBA* are not particularly helpful in distinguishing on the basis of "contributions" versus "special payments". While it is true that s. 4(2)(*c*) of the Regulations refers to "special payments" without, as in subss. 4(2)(*a*) and (*b*), indicating these are contributions, it is also true that s. 4(3)4 refers to "employer contributions for a special payment." I also note that s. 4(1) refers to a contribution "both in respect of the normal cost [that is, a regular payment] and any going concern unfunded actuarial liabilities" [i.e., special payments]. I conclude that, as is the case with so much technical legislation, particularly if it has been patchworked, the language of intent has simply not been fully coordinated. The *PBA* and Regulations thereunder are legislation which is not designed for persons not actively working in the field to tread in with any comfort.

25 However, it should be noted that s. 76(1) of the *PBA* is segregated into two parts, (*a*) and (*b*). Section 76(1)(*b*) appears to deal with special payment requirements envisaged by "going concern assets", "going concern liabilities", "going concern unfunded", "actuarial liability", and "going concern evaluation". This is so especially when "going concern liability" is said to mean "the present value of the accrued benefits of a pension plan determined on the basis of a going concern valuation" [s. 1, *PBA Regs.*]. Such going concern valuation is one that is required in the triennial report as set out in s. 11 of the regulations. Section 76(1)(*b*)(ii) appears to pick up the concept of the unfunded liability that was to have been made good by the special payments. Section 76(1)(*b*) is then to be contrasted with s. 76(1)(*a*), which deals with payments which are "due or that may have accrued" but have not yet been paid into the pension fund. This contrast implies that the special payments are not either due or accrued, as otherwise s. 76(1)(*b*)(ii) would be redundant. Section 5(1) of the Regulations speaks of the special payments being required to "amortize" a "going concern unfunded actuarial liability. ..." The *Oxford (Shorter) Dictionary*, 3d ed. (1988), reprinted, defines "amortized" as "to extinguish a debt, etc. usually by means of a sinking fund." Thus it denotes a setting aside of the moneys, not payment. It is also evident that such special payments in a going concern situation may fluctuate depending

on the investment results of the pension fund and the employer's ongoing contributions, together with the es timated demands on the fund by the beneficiaries. As of the date of crystallization being the wind-up date, the situation in the pension plan may be (significantly) different from that set forth in the last triennial report. At that time (or rather as of that time) it will be known what are the assets in the fund and the liabilities to be set against such funds by those beneficiaries who are then established as being legally entitled to claim.

26 It therefore appears to me that the deemed trust provisions of subs. 58(3) and (4) only refer to the regular contributions together with those special contributions which were to have been made but were not. In this situation, that would be the regular and special payments that should have been made but were not (as reflected in the report as of December 31, 1988), together with any regular or special payments that were scheduled to have been made by the wind-up date, July 13, 1990, but were not made. This is contrasted with the obligation of Usarco to fully fund its pension obligations as of the wind-up date pursuant to s. 76(1). It is recognized in these circumstances, however, that the bank will have a secured position which will prevail against these additional obligations as to the special payments, which have not yet been required to be paid into the fund. Sadly, it is extremely unlikely there will be a surplus after taking care of the bank to allow the pension fund to be fully funded for this (the likelihood being that the wind-up valuation of assets and liabilities of the pension fund will show a deficiency).

27 On that basis, I believe that there is merit in the bank's position that s. 58(4) takes into account those employee contributions (regular and special payments) which are developing, but not yet, but for that subsection, required to be paid into the pension plan. See Canadian Institute of Chartered Accountants, *Terminology for Accountants*, 3d ed. (C.I.C.A.: 1983), at p. 5, where "accrue" is defined as "in accounting, to record that which has accrued with the passage of time in connection with the rendering or receiving of service (e.g., interest, taxes, royalties, wages), but the payment of which is not enforceable at the time of recording." Section 59(1) states: "Money that an employer is required to pay into a pension fund accrues on a daily basis." Therefore, in my view the trust extends to the amount that Usarco was obligated to pay into the pension fund, prorated to July13, 1990.

28 It also seems to me that s. 59(2) of the *PBA* deals with the question of interest. It states: "Interest on contributions shall be calculated and credited at a rate not less than the prescribed rates and in accordance with prescribed requirements." This in my view means that interest is to be paid on contributions that are unpaid. I base this on the fact that contributions which are paid will generate income based upon what investments are in fact made (and could be interest, dividend, or other basket clause income), and secondly, that this obligation seems to relate to the obligations of the employer set out in the other part of the section (i.e., s. 59(1)).

29 There is then to be an order in the following terms:

(1) An order granting the administrator leave to bring this motion as per the order of Borins J. dated October 11, 1990.

(2) An order directing the receiver to pay the administrator an amount of money equal to the regular and special payments required to have been made but not yet paid into the pension plan, prorated to July 13, 1990, together with interest at the prescribed rate as set out in s. 59(2) of the *PBA* on all unpaid amounts from the date such were due to, and including the date of payment under this order. Counsel should be able to work out these amounts with their respective pension consultants, but if they are unable to do so, they may speak to me further.

(3) As to the question of costs, the receiver took the position that it was merely a stakeholder, and asked for its costs in the amount of $3,500. I award the receiver costs in that amount, payable out of the funds that it holds. As between the administrator and the bank, there were mixed results. It is also to be noted that apparently the question of the non-current, unfunded liability was a novel one. Balancing these factors together with the additional factor that the bank did not wish to proceed with the bankruptcy matter until a time convenient to it (if at all), I am of the view that the administrator should have part of its costs payable by the bank. I estimate those related to the current, unfunded liabilities as being $3,500. In accordance with the usual procedures, costs are to be payable forthwith.

TAB 8

1922
March 2, 3.
May. 2.

THE HYDRO-ELECTRIC POWER COMMISSION OF ONTARIO AND THE ONTARIO POWER COMPANY OF NIAGARA FALLS (PLAINTIFFS) ..... } APPELLANTS;

AND

JOHN JOSEPH ALBRIGHT (DEFENDANT) ..... } RESPONDENT.

ON APPEAL FROM THE APPELLATE DIVISION OF THE SUPREME COURT OF ONTARIO

Contract—Purchase of shares in company—Mortgage on company property—Security for bonds—Covenant to provide sinking fund—Earnings for calendar year—Payments at fixed date—Payments "accrued but not yet due"

As security for its bond issue the Ont. P. Co., in 1903, gave a mortgage of all its property to a trust company and agreed to provide a fund to redeem said bonds by paying, on the first of July in each year from 1903, one dollar for each electrical horse power sold and paid for during the preceding calendar year. In 1906 it gave another mortgage to secure debentures and again agreed to provide a sinking fund on the same terms and conditions except that the rate was twenty-five cents per h.p. payable out of net earnings. In 1917 the Hy. El. Com. entered into a contract with A. (acting for himself and other shareholders) to purchase ninety per cent of shares in the Ont. P. Co. and as much of the remaining ten per cent as A. controlled when the sale was completed. In this contract A. covenanted that when the sale was completed he would leave with the Ont. P. Co. a sum estimated by him to be equal to " * * sinking fund payments on the bonds and debentures * * * which shall have accrued but shall not be due at the time for completion." The time for completion was fixed at Aug. 1, 1917. On that date A. left with Ont. P. Co. a sum representing the power sold and paid for during the preceding month of July.

PRESENT:—Idington, Duff, Anglin, Brodeur and Mignault JJ.

DUFF J.—The majority of the Appellate Division has held that the sinking fund payments are, for the purposes of the agreement of April, 1917, to be treated as accruing *de die in diem* between the dates fixed for payment and as apportionable accordingly. This, it is not seriously disputed, involves the attribution to language giving rise to the dispute of an unusual and unnatural meaning. It is the basis, indeed, of the respondent's argument that these payments accrue due as an entirety on the date of payment and that there is not in the interval any accrual in any sense known to the law and that accordingly, apart from some special understanding that they should be considered apportionable for the purposes of the agreement out of which the dispute arises, they are not apportionable. I am convinced that the language of the clause in question is perfectly sensible with reference to the subjects to which it relates, the interest and sinking fund payments dealt with, and applying the language of the clause in its ordinary and well understood meaning the appellants have established their contention with reference to the first trust deed but have failed to establish it with reference to the second.

The controversy concerns the effect of the words

> interest and sinking fund payments on the bonds and debentures of the Power Company and the Transmission Company mentioned in Schedule D which shall have accrued but shall not be due at the time for completion

I agree with the argument presented on behalf of the respondent that we must be informed of the provisions of the instruments dealing with the payments for interest and sinking fund here referred to in order to ascertain the meaning and effect of the words "shall

1922

THE HYDRO-ELECTRIC POWER COMMISSION OF ONTARIO v. ALBRIGHT.

Duff J.

have accrued but shall not be yet due". But the object of looking at these instruments, it must be observed, is to ascertain the meaning expressed by the words themselves in the context in which they appear having regard to the particular circumstances with reference to which they are used. The subjects of this provision are such interest and sums payable for the purpose of a sinking fund as shall have accrued but shall not be due at the time mentioned; and in order to apply the provision you must ascertain what interest and what sums of the character mentioned fall at the specified time within the described category—the category defined by the words

> interest and sinking fund payments * * * accrued * * but not yet due.

The word "due" in relation to moneys in respect of which there is a legal obligation to pay them may mean either that the facts making the obligation operative have come into existence with the exception that the day of payment has not yet arrived, or it may mean that the obligation has not only been completely constituted but is also presently exigible. That it is used in the latter sense in the present instance is perfectly clear—otherwise the contrast expressed between payments "accrued" and payments "due" would, especially in the case of interest, be patent nonsense. The most natural meaning of such a phrase as "accrued payments" would be, and standing alone it would *prima facie* receive that reading, moneys presently payable; but the word "accrued" according to well recognized usage has, as applied to rights or liabilities the meaning simply of completely constituted —and it may have this meaning although it appears from the context that the right completely constituted

or the liability completely constituted is one which is only exercisable or enforceable *in futuro* —a debt for example which is *debitum in praesenti solvendum in futuro*. It is in this sense that it has been widely applied to express the fact that such a liability has been created in relation to a sum of money, part of a whole (made up of an accumulation of such parts) which is not to be payable until a later date, and it is in this sense that it seems to be used in the clause before us.

I fear I must, in view of the arguments advanced on behalf of the respondent and of the opinions expressed in the Appellate Division to which I shall refer with more particularity later, elaborate a little this point as to the meaning of the word "accrued." Generally sums received as rent, for example, and other sums of money payable periodically at fixed times are not, apart from statute, apportionable unless by reason of express provision or by implication an intention is manifested that they should become due *pro rata* from day to day. This intention is sometimes implied from the purpose of the payment as for instance in the case of charges for the maintenance of children which, though payable at fixed times, are considered to accrue from day to day because intended for the daily maintenance of the children. *Hay* v. *Palmer* (1). So in the case of interest where the interest payable on money lent was payable at fixed periods, it was held none the less to become due *de die in diem* and this upon the ground that the creditor might call in his capital at any time and interest was considered to be earned and to become due each day as the price of the creditor's forbearance. *Wilson* v. *Harman* (2);

(1) 2 P. Wms. 502.

(2) [1755] 2 Ves. Sen. 672 at p. 673.

1922

THE HYDRO-ELECTRIC POWER COMMISSION OF ONTARIO v. ALBRIGHT.

Duff J.

Hay v. *Palmer* (1); *Pearly* v. *Smith* (2); *Ex parte Smyth* (3). And this conception of the contract to pay at a specified date interest on money lent—that the sum payable on the date fixed was an accumulation of sums which had accrued *de die in diem* (a day according to a familiar notion being treated for this purpose as an indivisible unit)—came to be accepted as corresponding with the true nature of such a contract even when the principal, being itself payable at a fixed date, would not be called in at the discretion of the creditor. In *In re Rogers Trusts* (4) Kindersley V. C. declined, after investigating the practice in the master's office, to give effect to an argument that the principle was confined to those cases where the creditor was entitled to recall his principal at pleasure.

And the form of words employed to express the idea that interest reserved as payable on a fixed date becomes due from day to day (because earned by forbearance of principal) has varied little since Lord Hardwicke's time. Lord Hardwicke himself used the phrases "accrues every day" in *Pearly* v. *Smith* (2) and "becomes due from day to day" in *Wilson* v. *Harman* (5); Mr. Swanston in his note to *Ex parte Smyth* (3) "accruing *de die in diem*" and "becomes due *de die in diem*"; and Kindersley V. C. at page 340 in *Re Rogers Trusts* (4), says

> the interest payable on the debentures though payable half yearly is not an entirety but an accumulation of each day's interest which accrues *de die in diem* and which though not presently payable is still due.

An accurate writer, Mr. Leake, speaking of interest upon debts payable at fixed periods says it is considered to "accrue due". Leake, Uses and Profits of Land, page 447.

(1) 2 P. Wms. 502.
(2) [1745] 3 Atk. 261.
(3) [1815] 1 Swan. 337 at p. 357.
(4) [1860] 1 Dr. & Sm. 338 at p. 341.
(5) 2 Ves. Sen. 672.

TAB 9

ESSENTIALS OF
CANADIAN LAW

PENSION LAW

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6) Statutory Deemed Trust

a) Introduction

The *PBA* establishes a statutory deemed trust with respect to contributions owing, but not yet remitted, to the pension fund.[67] The purpose of the deemed trust is to exempt contributions owing to a pension plan, and which are held by an employer, from being seized or attached by the other creditors of the employer. Importantly, the deemed trust applies only to contributions not yet remitted to the pension fund—it does not make the pension fund itself, *per se*, impressed with a trust.[68] Nor does the deemed trust apply with respect to other assets of the employer that are not associated with pension contributions.

b) Application

Generally, the deemed trust operates in an ongoing plan and on wind up and applies both with respect to money held by an employer for employee contributions prior to deposit in the pension fund and in respect of the employer's share of its contributions that are due, but not yet paid. Amounts equal to the required contributions are deemed to be held in trust by the employer until paid into the pension fund. The trust extends over these assets, whether the contributions are commingled in the general revenue accounts of the employer or kept in a separate account.[69] The statutory deemed trust also extends to the interest accruing on employer and employee contributions that are owing, but not yet remitted, to the pension fund.[70]

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67 *Ibid.*, ss. 57(1)–(4). See also Alberta (*AEPPA*, s. 40.1).

68 *Crownx Inc. v. Edwards* (1991), 7 O.R. (3d) 27 (Gen. Div.), aff'd (1994), 120 D.L.R. (4th) 270 (Ont. C.A.). It should be observed that in an earlier Ontario court decision, the court stated that "it is common ground that pursuant to s.23(3) of the Act [the deemed trust provision in the pre-1987 *PBA*] the Plan is a trust:" see *Re King Seagrave Ltd. and Canada Permanent Trust Co. et al.* (1985), 51 O.R. (2d) 667 (H.C.J.), aff'd in the result [1986] O.J. No. 2124 (C.A.). However, in that case, unlike in *Crownx*, not much turned on this finding given the court's principal conclusion in *King Seagrave* that the plan in that case was subject to a true trust based on the application of common law principles. In any event, the pension fund may not be seized nor attached by creditors of the employer as it does not form part of the assets of the employer: see Chapter 5, section C(7).

69 *PBA*, s. 57(6).

70 *Ibid.*, ss. 58(1) & (2) and *Usarco*, above note 40. See, however, *Ivaco Inc. (Re)* (2005), 47 C.C.P.B. 62 at para. 13 (Ont. S.C.J.), where the court distinguished its earlier decision on *Usarco* on the facts and declined to give effect to the deemed trust on the basis that in the earlier decision, "while there was a bankruptcy petition outstanding at the time of the motion, no one was pressing it forward,"

The *PBA* does not expressly state whether a funding deficiency on the wind up of a pension plan is secured by the deemed trust, but it appears that the deemed trust is intended to apply to the deficiency to the extent it relates to employer contributions and remittances due and owing to the pension fund on wind up, but which have not been paid.[71]

c) Limitations

There are a number of important limitations on the application of the statutory deemed trust. First, the deemed trust only extends to "accrued" contributions. This includes the regular, "normal cost," contributions together with any "special payment" (that is, contributions required to fund a plan deficit) which were required to have been made by the employer, but were not. The deemed trust does not extend to the obligation of an employer to fund pension obligations that have not yet become due or which "crystallize" only upon the wind up of the pension plan. In these circumstances, a creditor will have a "secured position which will prevail against these additional obligations ... which have not yet required to be paid into the fund."[72]

Secondly, the statutory deemed trust does not exempt pension contributions in the hands of an employer from being made available for distribution among an employer's creditors in bankruptcy and insolvency proceedings.[73] Although section 67(1)(a) of the *Bankruptcy and Insolvency Act* (*BIA*)[74] exempts property held by the bankrupt "in trust" for another person from being divisible among creditors, a provincially-created statutory deemed trust (such as the *PBA*) is not operative for the

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whereas "in the present case ... there are major creditors who wish to proceed forthwith—and for the reason that such a bankruptcy will enhance their position (i.e. the pension deficit claims will become unsecured and rank *pari passu* with the other unsecured claims)." The Ontario Court of Appeal has granted leave to the Superintendent to appeal the decision in *Ivaco Inc. (Re)*. See also *General Chemical Canada Ltd. (Re)*, [2005] O.J. No. 5436 (S.C.J.), following *Ivaco Inc. (Re)*.

71 *PBA*, s. 75(1)(a) and *Usarco*, *ibid.*

72 *Usarco*, *ibid.*

73 *Ivaco Inc. (Re)*, above note 70. The court also noted another limitation in that "there is no provision in [the *PBA*] that the monies be paid out to the pension plan at any particular time" (para. 17). As such, even though the deemed trust operates prior to bankruptcy, if it is not acted upon until after bankruptcy, "those deemed trusts may be defeated, in the sense of being inoperative to give a priority, in the event of a bankruptcy. The *BIA* does not contain any provision that the priority position is maintained in a bankruptcy." See also *British Columbia v. Henfrey Samson Belair Ltd.*, [1989] 2 S.C.R. 24.

74 R.S.C. 1985, c. B-3, as amended.

purposes of the *BIA*, unless the trust, in addition, "has all the requisite elements of a common law trust."[75] As explained:

> While in a non-bankruptcy situation, the [employer's] assets are subject to a deemed trust on account of unpaid contributions and wind up liabilities in favour of the pension beneficiaries by s. 57(3) of the *Pension Benefits Act* (Ontario), in a bankruptcy situation, the priority of such a statutory deemed trust ceases unless there is in fact a "true trust" in which the three certainties of trust law are found to exist, namely (i) certainty of intent; (ii) certainty of subject matter; and (iii) certainty of object.[76]

If, therefore, an administrator or employees can establish that a true trust extends over the assets of an insolvent employer, those assets will be exempt from attachment by creditors and a proof of claim on behalf of employees may be allowed. Generally speaking, "[f]or these three certainties to be met, the trust funds must be segregated from the [employer's] general funds."[77] It is important to observe that for certainty of subject matter to be met, the trust funds must be "identifiable" and "traceable.". Where, prior to a bankruptcy, an employer has failed to remit to the pension fund employee pension contributions that it deducted from payroll and, instead, has commingled the contributions with its general revenues and used them for business operating expenses, the contributions become converted funds that are no longer identifiable and traceable. In such circumstances, the pension contributions lose their character as trust property held by a bankrupt and a claim by employees to recover their funds will be disallowed by the trustee in bankruptcy.[78]

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75 *Edmonton Pipe Industry*, above note 60 at para. 41. Because bankruptcy is a matter under federal jurisdiction, provincial statutory deemed trusts (such as those in the *PBA*) that do not conform to "general trust principles" cannot operate "to reorder the priorities in a bankruptcy." Therefore, although deemed trusts are effective in accordance with the provincial legislation when a person or business is solvent and operating, upon bankruptcy "the funds that are subject to a deemed trust, but are not held in accordance with general trust principles, will not be excluded from the property of the bankrupt under s. 67(1)(a) of the BIA and will be distributed in the priority prescribed by the *BIA*:" see *GMAC Commercial Credit Corp. Canada v. TCT Logistics Inc.* (2005), 74 O.R. (3d) 54 at para. 15 (C.A.). See also *British Columbia v. Henfrey Samson Belair Ltd.*, above note 73; *Usarco*, above note 40.

76 *Ivaco Inc. (Re)*, above note 70 at para. 11.

77 *Ibid.*

78 *Re Graphicshoppe Ltd.*, [2005] O.J. No. 5184 (C.A.), rev'g (2004), 74 O.R. (3d) 121 (S.C.J.). Supporing the court's reasoning was the fact that prior to the date

Thirdly, a bank's security under section 178 of the *Bank Act*,[79] both prior to and after an employer's bankruptcy, has priority over any assets impressed by the *PBA*'s statutory deemed trust. Pension benefits do not fit into the definition of "wages, salaries, commissions or compensation" owed to employees, as defined in section 107 of the *BIA*[80] and, therefore, an employee's pension claim retains the character it held prior to bankruptcy, that is., an unsecured claim.[81]

Recently, Parliament has enacted the *Wage Earner Protection Program Act*[82] (Bill C-55). This legislation amends the *BIA* and the *Companies' Creditors Arrangement Act*[83] (*CCAA*) to provide that pension contributions owing, but not yet remitted to the pension fund at the time of a bankruptcy or receivership, will have priority status, ranking above secured creditors.[84]

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of the employer's bankruptcy, the employer's account had a negative balance and therefore, none of the employee contributions remained intact. In a strong dissent, Juriansz J.A. held that the employees' trust claim should be allowed, as there was "no doubt that the pension contributions were the employees' money, and it is conceded that [the employer] held that money in trust upon deducting it from the employees' pay." In the minority's view, the pension contributions were an "indivisible asset" that could be traced to the employer's general account, based on the principle that "the mere commingling of trust funds with the trustee's own funds does not destroy a trust and, as such, does not in itself eliminate a beneficiary's right to claim a proprietary remedy" (paras. 65, 66 and 105). See also generally, *Edmonton Pipe Industry*, above note 60 and *GMAC Commercial Credit Corp. Canada v. TCT Logistics Inc.*, above note 75.

79 R.S.C. 1985, c. B-1, as amended.

80 Above note 74.

81 *Abraham v. Coopers & Lybrand Ltd.* (1998), 158 D.L.R. (4th) 65 (Ont. C.A.). This interpretation has not gone uncriticized. See the strong dissent in *Abraham* by Laskin J.A., who focused on the public policy reasons to prefer employee pension contribution claims over bank claims (at 90–91):

> It seems to me to be unjust on policy grounds, and contrary to "the realities of the arrangement" for the bank to permit its borrower to carry on business and thus enhance the value of its security and then deny compensation to those responsible for its enhancement. Workers improve the value of inventory by their labour and services. The court in *Armstrong*, understandably, sought to avoid a result that permitted the bank to claim the improved property without compensating those workers.

82 S.C. 2005, c. 47 (Royal Assent 25 November 2005).

83 R.S.C. 1985, c. C-36.

84 The relevant amendments come into force on a date to be proclaimed by order of the Governor in Council: *Ibid.* s. 141. These amendments are not yet in force.

TAB 10

Pension Management In Insolvency and Restructuring – What is at Stake?

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Presented at the

Insight 3rd Edition Commercial Insolvency & Restructuring at Toronto on September 19 & 20, 2005

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Introduction

Pension deficits and their treatment in restructuring cases have become a dominant issue for many debtor companies. In certain circumstances, the ability of companies to successfully restructure will depend on how they deal with pension funding obligations. The purpose of this paper[1] is to identify and briefly review significant pension matters that should be resolved in the context of corporate reorganisations and in particular corporate restructurings in an insolvency context.

Part I of this paper provides a general overview of the relevant pension considerations in a corporate reorganisation. Next, Part II discusses the specific pension issues that arise in a merger and acquisition context. Finally, Part III takes a closer look at how pension concerns have been addressed under a restructuring in insolvency. This examination ultimately points to the emergence of pension considerations as important to a number of stakeholders and a key to a successful restructuring.

Part I – Pension Overview

1. Scope

The focus of this paper is on a corporation conducting business in Ontario and subject to the laws applicable therein including the *Pension Benefits Act* (Ontario) (the "OPBA"), the regulation thereunder (the "OPBR")and the *Income Tax Act* (Canada) (the "ITA"). Although the paper will

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[1] Part I & II of this paper is an update of the paper entitled Pension and Other Employee Benefit Obligations in Corporate Reorganisations delivered at the 2005 Federated Press Taxation of Corporate Reorganisations Conference in January of 2005. The author wishes to acknowledge the assistance of McCarthy Tétrault colleagues Stephanie Smith, Lorraine Allard and Gareth Gibbins in preparation of the earlier paper. The author also wishes to thank Gareth Gibbins and Tony Kurian for their contribution to Part III of this paper.

raise issues which are relevant for non-Ontario businesses, this paper is not intended to address the subtle differences in federal or other provincial legislation applicable to pension and benefit matters nor to the differences in common law approaches in other jurisdictions.

For the purposes of this paper, a corporate reorganisation will include an amalgamation, a share sale or purchase, an asset sale or purchase, an event of significant downsizing and insolvency.

The paper will be limited to discussion of employer sponsored registered pension plans and non-registered or supplementary pension plans (including retirement compensation arrangements ("RCAs")). Welfare benefit plans, stock or phantom stock-based programs along with cash compensation, including severance, will not be addressed in this paper.

2. Background

(a) Types of Benefits Plans Provided by Employers

Benefits programs that may be provided by employers can be characterized as falling under one of two possible headings – defined benefit ("DB") or defined contribution ("DC"). A DB program is one in which the ultimate benefit is known or at least determinable by means of the terms of the program and other factors but the cost of delivering the final benefit is unknown. A classic example of a DB program is a "flat benefit" registered pension plan ("RPP"), common in unionised environments, in which a pre-determined annual or monthly amount of pension is payable from the plan for each year of service. Accordingly, the terms of such a registered pension plan will provide that the basic retirement benefit is, for example, $40.00 per month for life starting at age 65 for each year of recognised service and a participant in such a plan who has been a member of the plan for 30 years will receive a monthly pension of $1,200.00 for life.

In this kind of plan, the amount of a participant's pension is determinable once one knows both (a) the level of monthly benefit promised and (b) the number of years of recognised service the participant has accumulated – thus the benefit is "defined". However, the cost of providing the benefit is unknown since it depends on a variety of factors (e.g. the benefit level that will be in effect at retirement; the precise date the pension will commence; the length of time the pensioner will live and the length of time his or her spouse will live if there is a survivor component; the rate of return on plan assets in the period prior to retirement; the rate of return on plan assets provided after retirement, where the employer does not purchase annuities at the employee's retirement from an insurer to pay the pensions; and the prevailing interest rate available at the time the annuity is purchased). Rather, the cost is simply predicted in advance using actuarial advice which recommends, from time to time, contributions based on estimates of the foregoing factors.

In contrast, a DC program is one in which the amount of employer and, if applicable, employee contributions is known and the benefits are simply those which can be purchased with the accumulated contributions. An example of this would be a DC registered pension plan where both the employer and the employee contribute 5% of salary (both subject to limits under the applicable tax legislation), the contributions are then invested but it is uncertain as to the amount of lifetime pension that the contributions may ultimately yield based on investment return in the pre-retirement period and the cost of acquiring an annuity at the time of retirement.

In the context of corporate reorganisations, shareholders and management of corporations are typically interested in employee benefit plans for two main purposes. The first is to ensure that proper administrative steps are taken in respect of the planned reorganisation to ensure that there is no unintended disconnect with the programs which will create employee relations problems or

exposure to claims arising from same by employees. The second is to identify existing liabilities with respect to current employee benefits and, in particular, any unfunded or under-funded liabilities connected to the programs. Therefore, DB programs are typically those which are the subject of greater attention, review and concern in corporate reorganisations than are DC programs. However, as may be appreciated from the Enron situation, DC programs are not immune from problems. For example, there are issues emerging from promotion of the employer's shares as an investment alternative in such programs and the unsurprising fall out when both the employer fails and the employee's corporately sponsored savings program account has been reduced to a fraction of its earlier value.

(b) Retirement Programs – RPPs and RCAs

As noted above, probably the most recognisable form of DB arrangement in retirement savings is the DB RPP which may take the form of a flat benefit plan as described above or a program which bases the benefit on annual or average annual remuneration. In all cases, the hallmark of such a program is that the quantum of the benefit is determined or calculable by reference to a formula and is not based upon the contributions to the programs. Some programs require employee contributions but, ultimately, in offering the program the employer has made a promise to the employee to deliver a particular amount of pension and if the assets that have been allocated from time to time to the pension plan to meet the promise are insufficient to provide that amount, it will be the employer's obligation to provide additional assets to meet the promise.

Pension standards legislation requires that the employer or plan administrator cause regular actuarial valuations of the funded position of a DB RPP program to be completed and that

contributions be made in accordance with pension standards laws so that the benefits are likely to be satisfied from the pension fund. However, there is a somewhat common misconception that employers are required to ensure that the RPP is, at all times, fully funded. That is simply not the case and pension standards legislation only serves to require that current service contributions be made on a reasonable basis and that any other unfunded liabilities or solvency deficiencies be eliminated by adopting a compliant amortisation program (these technical pension issues are discussed further in Part III of the paper). If investment performance is regularly below the actuarial estimates, then the fund will fail to grow to the level necessary to meet the promised benefits. Contributions that are required by pension standards legislation will generally be tax deductible.

Key features of a properly administered DB RPP are:

- the plan provides a formula to determine the benefits
- the employer must contribute to a pension fund and the employees may be required to contribute
- contributions are held in a tax-deferred trust – tax being payable only on amounts paid from the trust to the plan participants (or the employer)
- employee and employer contributions are deductible from the contributor's income and employees receive no income inclusion for employer contributions
- the plan must be registered under both tax laws and pension standards law.

Because of the relatively modest limits on so-called "tax assisted retirement savings" in Canada,[2] many employers now provide a supplementary pension (often referred to as a "Supplemental Executive/Employee Retirement Plan" or SERP) which provides benefits that would otherwise have been provided under the terms of the employer's registered pension plan were it not for the tax limits on benefits payable from such a registered plan. For 2005, a pension payable from a registered pension plan cannot exceed $2,000 for each year of credited service thereunder[3]. For a 30 year employee, current limits allow for an annual pension of approximately $60,000. In the event that the employer's pension program is designed to replace, for example, 60% of an individual's pre-retirement earnings and the individual earns $200,000 per year, the registered pension plan would only be able to provide one half of the anticipated $120,000 annual pension. An equal amount would, therefore, be provided out of the SERP. If the SERP is funded, it will most likely take the form of an RCA and will be subject to the rules dealing with RCAs.

An RCA[4] is essentially a funded (or secured) pension plan that does not otherwise qualify as a specified type of "plan" defined under the ITA. RCA is defined in the ITA as follows:

> "retirement compensation arrangement" means a plan or arrangement under which contributions (other than payments made to acquire an interest in a life insurance policy) are made by an employer or former employer of a taxpayer, or by a person with whom the employer or former employer does not deal at arm's length, to another person or partnership (in this definition and in Part XI.3 referred to as the "custodian") in connection with benefits that are to be or may be received or enjoyed by any person on, after or in contemplation of any substantial change in the services rendered by the taxpayer, the retirement of the taxpayer or the loss of an office or employment of the taxpayer, but does not include
>
> (a) a registered pension plan,

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[2] See discussion under section 2(c)(v) of this paper, below, for a detailed history of the maximum pension rule.

[3] The 2005 Federal Budget proposed a modest increases to RRP contribution limits which would increase the limit to $2,111 in 2006, $2,222 in 2007, $2,333 in 2008 and $2,444 in 2009. From 2010 onward the limit would be indexed to the increase in the Average Industrial Wage.

[4] The following is, substantially, an excerpt from Greg Winfield, "Funding SERPs: The Current Available Options" dated May 10, 2001 (2001, The Canadian Institute, Toronto).

(b) a disability or income maintenance insurance plan under a policy with an insurance corporation,

(c) a deferred profit sharing plan,

(d) an employees profit sharing plan,

(e) a registered retirement savings plan,

(f) an employee trust,

(g) a group sickness or accident insurance plan,

(h) a supplementary unemployment benefit plan,

(i) a vacation pay trust described in paragraph 149(1)(y),

(j) a plan or arrangement established for the purpose of deferring the salary or wages of a professional athlete for [the athlete's] services as such with a team that participates in a league having regularly scheduled games (in this definition referred to as an "athlete's plan"), where

(i) the plan or arrangement would, but for paragraph (j) of the definition "salary deferral arrangement" in this subsection, be a salary deferral arrangement, and

(ii) in the case of a Canadian team, the custodian of the plan or arrangement carries on business through a fixed place of business in Canada and is licensed or otherwise authorized under the laws of Canada or a province to carry on in Canada the business of offering to the public its services as trustee,

(k) a salary deferral arrangement, whether or not deferred amounts thereunder are required to be included as benefits under paragraph 6(1)(a) in computing a taxpayer's income,

(l) a plan or arrangement (other than an athlete's plan) that is maintained primarily for the benefit of non-residents in respect of services rendered outside Canada,

(m) an insurance policy, or

(n) a prescribed plan or arrangement,

and, for the purposes of this definition, where a particular person holds property in trust under an arrangement that, if the property were held by another person, would be a retirement compensation arrangement, the arrangement shall be deemed to be a retirement compensation arrangement of which the particular person is the custodian. [emphasis added]

Unless one attempts to re-characterise the nature of the payments under most kinds of funded or secured SERPs, the contributions made thereto will be made "in connection with benefits that are to be or may be received or enjoyed by any person on, after or in contemplation of ... the retirement of the taxpayer". While it is possible to parse through the definition and construct what is, in effect, a supplementary pension benefit that somehow skirts the definition of RCA

(e.g. by making the payments payable earlier than termination of employment or earlier than retirement), for most employers who have investigated the various funding vehicles, the RCA, like it or not, is the form of vehicle which is adopted to provide the funding or security of the SERP promise. Technically speaking, the definition operates such that if the corporation can fit the arrangement under the auspices of any of the other enumerated types of plans (e.g. RPP, employee profit sharing plan, employee trust), the arrangement will not be an RCA.

The general operation of an RCA is that employer contributions are immediately deductible to the employer (subject to the usual reasonableness test) but the employer must withhold 50% of the amount of its contribution and remit that as a refundable tax.[5] The refundable tax is held by the Canada Revenue Agency ("CRA") in a non-interest bearing account and the amount is refunded to the custodian as described below. The net amount contributed is paid to the "custodian" of the arrangement. The custodian is typically a trustee and therefore trust terminology will be used in this paper. The trust is also subject to a 50% refundable tax on its annual income and realised gains. However, the custodian's obligation to remit this refundable tax is reduced to reflect distributions made by the custodian on the basis of $1 for each $2 that has been distributed. Amounts distributed from the trust, whether to the RCA members or to the employer, are subject to tax in the hands of the recipient.

Although the RCA was meant to operate as an anti-avoidance measure and was initially viewed as a vehicle to avoid at all costs, it has become increasingly used by employers who find themselves obliged to provide funded benefits in order to keep senior employees content. Accordingly, it is now viewed as a necessary evil.

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5 The possibility of employee contributions to an RCA is ignored to simplify the description.

As it is not a "registered" plan, there are no investment restrictions on an RCA. Indeed, somewhat inventive strategies with respect to investments and otherwise have been developed for RCAs - principally the use of exempt life insurance policies or leveraging the RCA. However, it can be argued that it would be of some utility in an RCA to hold investments that will not produce annual income or dividends but will provide only capital growth such as insurance policies or growth stocks. In that way, the tax burden of refundable tax may be less onerous than would otherwise be the case.

Described in a simplified fashion, the employer contributions made to an RCA will all be subject to a 50% refundable tax but, subject to the usual reasonability test, will be deductible from the income of the employer in the year in which the contribution is made. Thus, in the event that a gross contribution of $100.00 is made to an RCA, $50.00 will ultimately reside in the refundable tax account established for the RCA and $50.00 will be held by the trustee. The trustee will be obliged to file a tax return for the RCA 90 days after year end in respect of the calendar year. The net income and realised gains of the trust are also subject to a 50% refundable tax. It is a result of both the refundable tax on employer contributions to RCAs and the ongoing 50% refundable tax on the net amount and gains of the trusts that the RCA compares unfavourably, in most observer's minds, to the RPP or other tax-deferred trust vehicle which it tops up. Some techniques to minimise the debilitating effect of the high tax rate are to hold securities which yield little in the way of dividends or income but that provide capital growth so that, if held for a reasonably long period time, the effects of the refundable tax are minimised. However, the negative tax effects of the RCA in respect of capital gains have become much more pronounced in the last 12 months with the substantial reduction in the capital gains inclusion rate together with our gradually falling federal and provincial personal income tax rates.

Recovery of the refundable tax is, generally speaking, made in one of three ways. While the trust is ongoing, the trustee will receive credit either in the form of a reduction in annual refundable tax to be remitted to the Receiver General or by way of refund from the refundable tax account relating to distributions made to beneficiaries of the trust at the rate of 50 cents for every one dollar of distribution.

The second way in which refundable tax may be refunded is by making the election permitted under subsection 207.5(2) of the ITA.. Provided the assets of the trust consist only of "cash, debt obligations, shares listed on a prescribed stock exchange, or any combination thereof", this election permits the trustee to elect, in the tax return, that the refundable tax be deemed to equal the "value" of such assets. Thus, any amounts in excess of that amount which are held by the Receiver General in the refundable tax account will be refunded to the trustee.

The final method to recover the refundable tax is a variation of the foregoing but simply occurs when the other assets of the trust have been totally disbursed therefrom and thus, there remain zero assets in the trust fund. At this point, a request can be made to recover the entirety of the refundable tax. The current administrative practice of CRA in respect of RCAs appears to permit recovery of this refundable tax by filing a tax return at any time. That is, there is no need to wait until the year end to file this tax return, and the officials at the Winnipeg office will process the return prior to waiting for the year end.

(c) Special Issues in DB Arrangements

There are certain features of benefits plans which may or may not exist from program to program which can be expected to result in greater complexity and risk of large unfunded liabilities,

depending upon the precise form of the reorganisation at issue. The most important types of these features are outlined below.

(i) Special Concerns for Retiree Pension and Non-Pension Liabilities

DB retirement programs may include both benefits from RPPs ("registered benefits") pension plans and benefits from SERPs ("non-registered benefits"). While registered benefits are always funded to some extent, partly due to the favourable tax regime and as a result of requirements of pension standards legislation, this is not true of non-registered benefits. Accordingly, while there is always some risk that an RPP may not be fully funded (e.g. as a result of adverse experience as against actuarial assumptions, recent benefit improvements, prevailing economic circumstances etc.) it is more likely than not that non-registered benefits will not be funded at all.[6] In the context of a corporate reorganisation, these unfunded liabilities merit specific attention as it will be appropriate for the purchaser to factor in such liabilities in determining the price it pays for the shares or the assets to be acquired.

In addition, there may be issues relating to tax deductibility of amounts paid to persons who were never employed by the purchaser. These concerns must be addressed where material unfunded liabilities for retirees are being assumed in an asset purchase transaction. Similarly, it may be useful to review the past dealings of an entity which is subject of a share purchase transaction or to determine whether any such liabilities exist as a result of prior transactions undertaken by the target corporation.

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[6] It has been reported that in recent surveys of Towers Perrin and Watson Wyatt conducted in 2000, that most SERPs remain "pay as you go". Towers Perrin is reported to have survey data disclosing that 67% of DB SERPs and 64% of DC SERPs remain unfunded (see Lyle Teichman, "Supplemental Employee Retirement Plans: An Overview of Supplemental Pension Issues in Canada" (2001, The Canadian Institute, Toronto)) while Watson Wyatt is reported to have concluded that 71% of all SERPs remain unfunded (see Patrick Longhurst, "How to Develop Your Organization's Funding Strategy" (2001, The Canadian Institute, Toronto)).

(ii) Change of Control Provisions

In the volatile commercial world in which we now live, it is becoming increasingly more common to institute change of control provisions as independent benefits – primarily those which would yield "parachute payments". Like severance programs, these are not included as a benefit plan for purposes of this paper. However, change of control provisions may also be added as features of regular benefits programs and when triggered yield (i) earlier vesting, (ii) requirements to prefund what are otherwise unfunded benefits or (iii) a requirement to provide a greater level of benefit than existed prior to the change of control. These features are "triggered" when any one of the events which gives rise to a change of control, as defined by the term adopted for the particular plan, occurs. Typically, this list includes acquisition of control[7] by a new shareholder but may also include other tests including a sale of a large portion of a corporation's assets.

Any corporation undertaking a share purchase (and even some asset purchases depending on the trigger events) must pay careful attention to the target corporation's benefits programs to determine whether change of control features exist and, if they do, what the precise effect will be so that the proper value can be placed on the shares or the assets. These kinds of stand alone programs or added features to existing benefits programs are often implemented either on the eve of a takeover or at a point in time when the corporation feels that it is vulnerable to be taken over. Accordingly, change of control features may be introduced to serve as so-called "poison pill" provisions. It is beyond the scope of this paper to investigate the possible merits or

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7 Various definitions of control are used, one common method is to adopt the terminology of the statute under which the corporation is incorporated.

challenges to such provisions, but it is worthwhile noting that, in reviewing these provisions, a purchaser may wish to verify the validity of the program or feature.

Finally, it should be noted that corporate re-organisations where a change of control provision in a SERP is unintentionally triggered by an "internal" re-organisation are not uncommon. In these circumstances it may be necessary to obtain waivers or consents from the SERP members to avoid having to fund the arrangement or call a letter of credit. Often, due to the internal nature of the event, the operation of the provision in the context is discovered late in the process and may cause embarrassment and even serious problems. Accordingly, early awareness of these provisions and, better yet, thoughtful design of the change of control feature when it is adopted is desirable.

(iii) General Surplus Considerations in Pension Plans Where No Downsizing

When dealing with registered pension plans, one should appreciate that pension plans may hold assets which exceed the liabilities at the date of the reorganisation. Various events giving rise to a corporate reorganisation may bring the fact of such a surplus into focus. For instance, in completing a share purchase transaction, there may be issues of how to value the surplus that exists in the registered pension plan(s) and whether some kind of price adjustment for the level of surplus existing on closing should be provided. Any purchaser who is, in fact, "paying" for surplus should investigate whether the surplus has a value to it in so far as the surplus may or may not be available to take so-called employer "contribution holidays" or given the terms of the plan or statutory and common law regimes existing in Canada from time to time to be withdrawn for the benefit of the target corporation.

These issues are also highlighted in asset purchase transactions where there may be a more obvious issue of a price increase to reflect surpluses being transferred from the vendor's pension plan to the purchaser's pension plan.

Finally, in the event that the corporate reorganisation is of an insolvency nature, this may give rise to a termination of an RPP. The rules in pension standards legislation governing distribution of all of the assets of the RPP may then require that the surplus be distributed entirely to the plan members or be shared between the plan members and the employer (or trustee in bankruptcy as the case may be) after completion of a consensual surplus sharing agreement and approval of the applicable regulatory authorities.

(iv) Surplus and Other Considerations in Downsizings

The issue of the distribution of pension surplus on partial wind ups of RPPs has received rare media and other attention over the last few years, culminating in the Ontario Court of Appeal landmark decision in *Monsanto*[8], which was recently upheld by the Supreme Court of Canada. In this section of this paper we will review and consider the implications of the *Monsanto* decision.

In Ontario, a partial wind up ("PWU") of an RPP is an event that will occur in one of two ways. The first is when the sponsor of an RPP voluntarily declares such an event to occur – and the plan sponsor has no direct, legislative direction or impediments to making such a declaration. The second way in which a partial plan wind up might occur is for the Superintendent of Financial Services (the "Superintendent") to declare the same. The Superintendent can make

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[8] *Monsanto Canada Inc. v. Ontario (Superintendent of Financial Services)*, (2004) 41 C.C.P.B. 106 (S.C.C.) on appeal from 32 CCPB 248 (Ont. C.A.) confirming (2001) 27 C.C.P.B. 82 (Ont. Div. Ct.) which reversed in part (2000) 23 C.C.P.B. 148 (F.S. Trib.) ("*Monsanto*").

such a declaration only in prescribed circumstances, and the OPBA provides that the Superintendent retains discretion not to make such a declaration even where the prescribed circumstances are found to exist. Such circumstances[9] generally occur when there is a "significant" decrease in the population of the active members of the RPP arising from involuntary terminations. Most typically this will occur in conjunction with downsizings undertaken by the employer, but may also occur in the event that a business is shut down at a discrete location, there is a plant closure. The rules in the OPBA are not crystal clear and have been the subject of some litigation, none of which has provided a broad set of principles as to what may constitute "significant" or what may or may not cause the Superintendent to exercise discretion to not order a PWU when the prescribed conditions are found to exist. It is beyond the scope of this paper to delve further into the issues surrounding the basis for a PWU order but it is sufficient to note that a larger downsizing (including plant closure) falls within the purview of "re-organisation" for the purposes of this paper and so it is possible that a re-organisation of that nature may trigger a PWU.

Background - Monsanto

The background to the Supreme Court decision in *Monsanto* is necessary before proceeding. In December of 1998 following a voluntary PWU of its RPP, the Superintendent proposed to refuse to approve the PWU report in respect of employees who had terminated employment with Monsanto Canada Inc. ("MCI") between December 31, 1996 and December 31, 1998. The *Monsanto* case is relevant for a number of significant pension standards and administrative law issues but for the purposes of this paper, the analysis is restricted to the issue of whether or not

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9 See subsection 69(1) of the OPBA.

subsection 70(6) of the OPBA requires that surpluses be distributed on PWU. That provision reads as follows:

> 70(6) On the partial wind up of a pension plan, members, former members and other persons entitled to benefits under the pension plan shall have rights and benefits that are not less than the rights and benefits they would have on a full wind up of the pension plan on the effective date of the partial wind up.

It should be noted that subsection 70(6) is unchanged since the OPBA took effect on January 1, 1988 and that prior versions of the legislation, dating back to 1969, contained largely analogous provisions. Nonetheless, neither the Superintendent nor her predecessors had ever issued an order which had the effect of requiring that surplus be distributed from an RPP on a PWU. Instead, when the Superintendent issued approval letters for wind up reports, and only in the period of a few years prior to *Monsanto*, a comment was added to the effect that the plan administrator was responsible for discharging the obligations under the OPBA with respect to the surplus attributable to the PWU. That is, no order requiring the surplus actually be distributed ever had followed such reports. However in December of 1998 such an order was issued to MCI.

MCI appealed the Superintendent's order to the Financial Services Tribunal (the "Tribunal") and, in a split decision, two of three panellists (the "Majority") favoured MCI's position and found that subsection 70(6) of the OPBA does not require that surplus be distributed on a PWU. One of the three panellists (the "Minority") concluded otherwise and found that the effect of the provision was to require that surplus be distributed. One of the significant areas of difference between the Majority and the Minority was the interpretation of the Supreme Court of Canada's (the "SCC") decision in *Schmidt v. Air Products of Canada Ltd.*[10] ("*Air Products*"). The

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10 [1994] 2 S.C.R. 211 (S.C.C.).

Majority concluded that the SCC's decision stood for the proposition that no surplus exists until an RPP is fully wound up, whereas the Minority determined that a PWU is a concept that creates a complete termination of the portion of the RPP relating to the affected employees and thus crystallizes surplus in the manner mentioned in the *Air Products* decision. The conclusions on this issue are a key area of departure in determining what the *Monsanto* decision will ultimately mean.

The Superintendent and a group representing terminated MCI employees appealed the Tribunal's decision to the Divisional Court and, in a brief decision dated March 19, 2001, the Divisional Court adopted the reasons of the Minority, but also noted that

> ... the result intended by the Legislature ought to be set out in language that is clearer than that presently contained in section 70(6) at the earliest reasonable opportunity. Until then, however, this judgment will serve to provide guidance as to what this Court considers the Legislative intention to have been.

The Divisional Court, characterising the issue as "critical", observed that the issue of distribution of surplus on a PWU was one that was not clearly dealt with in the OPBA and that language to more clearly reflect legislative intent should be added to the OPBA.

Court of Appeal Decision in Monsanto

On November 22, 2002, the Ontario Court of Appeal (the "OCA") released its decision in *Monsanto*. In a judgment containing more detailed reasoning than was found in the decision issued by the lower court, the decision of the Divisional Court was upheld. The OCA observed that on a full wind up of an RPP, the members have the right to require that the full surplus be distributed[11] – although it should be noted that this does not prejudge to whom the surplus is to

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[11] This arises, largely from the definitional framework of the OPBA wherein the terms "wind up" and "partial wind up" refer to the distribution of assets of the pension fund or that part of the pension plan being terminated and this is generally interpreted to mean all of the subject assets.

be distributed. The OCA asserted that the scheme of the OPBA is to deal with full wind ups and PWUs in a parallel manner and concluded that the legislation had, since a 1969 regulation, provided for similar rights on PWU as existed on full wind up. Because the distribution of surplus is a right on full wind up, the reasoning followed that it must be a right on PWU. The OCA also expressed the view that it was less complicated to deal immediately with the distribution of surplus in respect of the group affected by the PWU than would be the case later (i.e. if the matter was deferred to a full wind up). In addition, the OCA found that the decision of the SCC in *Air Products* was simply inapplicable to PWU cases as that case involved a full wind up and because it did not involve any statutory provisions, let alone a provision such as subsection 70(6) of the OPBA. Accordingly, the OCA found that the reasoning of the Majority of the Tribunal, when it relied on *Air Products* for support that there was no surplus to distribute on a PWU, was flawed.

It should be noted that one issue that was agreed on by the Majority and the Minority of the Tribunal was that annuities need not be purchased on the PWU of a plan to satisfy the obligations to those affected persons who chose a pension from the RPP. This element of that decision was not appealed by the Superintendent nor the former members. However, it would appear that the OCA's comments on the strong (if not exact) parallel of treatment of full and PWUs in the OPBA suggests that annuity purchases should be a requirement along with surplus distribution since distribution of all of the assets means simply that all assets leave the RPP.

The Supreme Court of Canada Speaks[12]

Regrettably for employers, the *Monsanto* decision, issued in late July 2004, upheld the decision by the OCA and determined that subsection 70(6) of the OPBA requires that if there is a surplus in the plan at the time of a PWU, then the portion of the surplus allocable to the plan members affected by the PWU ("Affected Members") must be distributed from the plan.

In reaching this conclusion, the SCC rejected policy arguments that its ruling could result in some plan members receiving less than full benefits from the plan while the Affected Members receive full benefits plus a distribution of surplus. It was argued that if the surplus that existed at the time of a PWU has subsequently eroded and a deficit now exits, members and pensioners left in the plan could find themselves receiving less that the promised pension should the employer become insolvent and unable to fund the pension plan. The SCC expressed sympathy for the Affected Members given that they have suffered a job loss. The SCC also seemed to adopt the view that a appropriate surplus distribution to the Affected Members is not prejudicial because there still exists a notional surplus for the remaining members and those remaining members are also protected by the funding requirements under pension standards law to deal with future deficits. Finally, the distribution of surplus was also found by the SCC to be consistent with the trust principles outlined in *Schmidt*. Following the SCC's rationale, when a partial plan wind up occurs, the portion of the actuarial surplus attributed to the Affected Members becomes an actual surplus to which they are entitled.

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12 The discussion of the SCC decision in *Monsanto* is largely based on the McCarthy Tétrault LLP Legal Update of September 2004 prepared by the Author.

Implications of Monsanto

The obvious result of the *Monsanto* decision is that on future PWUs surplus will need to be distributed under some kind of regime which may or may not involve "sharing" and which will, no doubt, evolve over time. However, the retroactive issues raised by *Monsanto* are very uncertain and very complex.

It is submitted that in order to properly implement the findings of the SCC, one must go back to the 1969 regulation referenced in the *Monsanto* decision and, starting from the effective date of that change, examine each and every PWU report for each RPP to determine if that PWU was in respect of any Ontario members and if surplus existed at the time of that PWU. If it did, then steps to properly distribute that surplus must be taken (see below for possible methodologies to determine the surplus). The same process must be followed through in each successive PWU report for such RPP. Of course, the distribution of such surpluses will mean that all of the subsequent valuations (including regular triennial reports, wind up reports, conversion reports, sale of business transfers, mergers reports, etc.) prepared in respect of the RPP – for both pension plan funding and for accounting purposes – will have been inaccurate and so these too will need to be adjusted and restated. This recreation of history, would be, without doubt, a massive undertaking that would require years, if not a decade, to resolve and will be very expensive.

In addition, the foregoing does not even take into account those events which were not voluntarily or otherwise declared as PWUs, but which might have constituted PWUs. Plan members or former members who now understand they may be entitled to some kind of distribution of surplus may wish to initiate reviews by the Superintendent of such potential events with a view to seeking a PWU order. The requirement to distribute surplus will bring with it greater likelihood of disputes as to the number and precise date of PWU events since

these may influence the size of surplus and the groups effected. Furthermore, the issue of a requirement to purchase annuities will also need to be taken into account. This has potentially greater affects than surplus distribution since not all PWUs involve a surplus but most will involve at least some members who elect pensions. As a practical matter, there may be difficulties in obtaining deferred annuities.

The upshot of the foregoing is that there will be no certainty in the operation and administration of defined benefit RPPs until all of the historic reports have been corrected and events requiring a surplus distribution and/or annuity purchase addressed.

There are two likely methodologies for establishing the amount of a PWU surplus to be distributed. The first is to accept that there has been a PWU event affecting the entire RPP and to measure the surplus at the time of the event, in a sense to "freeze" it, and then to require that that amount be distributed. This methodology will need to address the issue of whether the frozen amount should be increased or decreased with a rate of interest or otherwise during the period from the PWU date to the date of distribution. The second methodology is to view the PWU as creating a second RPP at the date of the PWU and to identify the assets attributable to this newly-created RPP distinct from the assets of the initial RPP. Since, in most instances, the assets allocable to the PWU, including the allocable surplus, were not separated from the other plan assets, this approach would result in the assets allocable to the second plan increasing or decreasing with the investment gain or loss incurred on the total fund over time. This latter approach may be favoured by many employers faced with PWUs in the late 1990's because the surplus assets to be distributed would "float" in value with investment performance and the employer may not be the guarantor of the surplus amount. However, it is conceivable that those affected by the PWU would argue that the plan administrator should have altered the investment

strategy for the PWU assets given that the assets should be distributed relatively quickly and a shorter term investment strategy was appropriate. If the first approach is adopted, the employer would, in effect and at a minimum, guarantee the value that existed at the PWU date. In this scenario, it is also possible that those affected by the PWU would be entitled to an increase in the value of the surplus assets on the theory that the plan administrator retains an obligation to invest the assets prudently until they are distributed. In any event, the regulators are going to have to give a great deal of thought to this issue and develop a sensible, coherent, comprehensive and (hopefully) fair policy.

Within one month of the SCC decision in *Monsanto*, Ontario's pension regulator (the "Financial Services Commission of Ontario" or FSCO) sent letters to a number of employers who had filed a PWU report prior to July 29, 2004, (the date of the SCC decision in *Monsanto*). These letters request an updated balance sheet and a timetable and proposal for dealing with any distribution of surplus related to the PWU. More recently, on March 22, 2005, FSCO released a brief report on partial wind ups in the post Monsanto era. Unfortunately, this report does little to alleviate the concerns and the uncertainty surrounding the Monsanto decision discussed in this section of the paper.

Notwithstanding the foregoing complexity produced by the *Monsanto* decision, quite possibly the most negative repercussion is that it produces opportunity for significant inequities among plan members to emerge. It is quite evident in recent years that many RPPs that were in surplus in the mid to late 1990's are no longer in surplus or have had their surpluses slashed significantly. The *Monsanto* result has the potential to turn the defined benefit RPP into a form of lottery. In this lottery, members who lose their jobs in a PWU and at a time when the RPP is perceived to be very well funded have the opportunity to benefit from the surplus that existed at

that time. Conversely, those members who terminate employment or retire in circumstances that are not a partial or full wind up and those employees who are included in a PWU which occurs during a period where the plan is not in surplus will not have that opportunity. In addition, and most importantly, should the RPP be fully wound up at a time where there are insufficient assets to fully provide the pensions and where the employer is insolvent, then (absent intervention of the Ontario Pension Benefits Guarantee Fund) the members involved in the full wind up would receive less than 100 percent of their basic pension benefits and, of course, no surplus. Unfortunately, these concerns were not founded to be persuasive by the SCC.

At this time, it is unclear whether and when there might be a legislative response to *Monsanto*. To the extent that there is no response, then employers undertaking corporate re-organisations which involve job losses of the nature that may trigger a PWU should take notice of the repercussions of the requirement to distribute surplus on a PWU. As the recent case law is unfavourable to employer claims to surplus in most instances, any requirement to distribute surplus on a PWU brings with it a significant likelihood that this means distributing it to the plan members. Therefore, most employers will first try to avoid having to distribute surplus and, if that cannot be avoided, then attempting to obtain value for same. Methods to avoid having to distribute surplus include, adopting a funding policy which is unlikely to give rise to surplus in the first place and if there is a surplus, trying to time the events such that the PWU date or dates occur when the surplus is at its relative lowest mark. In addition, it may be possible to negotiate with the employees to reduce severance payments in return for benefit enhancements or other surplus payments, although it remains to be seen if employees will accept this. Employer's who provide SERPs may wish to add as an offset to SERP benefits the value of any surplus distributed from the RPP.

(d) DC Arrangements

Just as there are DB RPPs, there may be DC RPPs (which, along with other savings arrangements are sometimes referred to as Capital Accumulation Plans or CAPs). As noted above, these programs feature monies contributed by the employer or the employee (within applicable tax limits) and the contributions are invested to produce a lump sum which may be used to buy an annuity or otherwise provide retirement income. In theory, these programs are less problematic for employers in the context of corporate reorganisations because there are no unfunded liabilities so long as the contribution obligations are satisfied. While this is correct, it would be unwise to believe that there is no potential exposure in connection with such plans. Without delving into the issue in detail, it should be noted that the investment of such plans is becoming a matter of greater scrutiny, both by the affected employees and by the regulators and therefore it would be unwise to assume that no liabilities may exist with respect to the assets once they are contributed.

Indeed, the Joint Forum of Financial Market Regulators (the "Joint Forum") released on May 28, 2004, a final version of the "Guidelines for Capital Accumulation Plans".[13] The Joint Forum is comprised of CAPSA, the Canadian Council of Insurance Regulators ("CCIR") and the Canadian Securities Administrators (the "CSA") who have been working together to improve and develop industry standards in respect of CAPs that are employer sponsored and provide for investment decisions to be made by the employees who participate in them. The guidelines are a response to the perception that CAPs, although they have been gaining in popularity, have not been the focus of regulators and CAP sponsors have been slow to recognise their fiduciary

13 This paper is available on CAPSA's website at www.capsa-acor.org.

obligations in this area. The guidelines were created to reflect the expectations of the regulators regarding the operating of CAPs, regardless of the regulatory regime applicable to the plan and were intended to support the continuous improvement and development of industry practices.

The guidelines outline the rights and responsibilities of CAP sponsors, service providers and CAP members with respect to setting up a CAP, investment information and decision-making tools for CAP members, introducing the CAP to CAP members, ongoing communications to CAP members, maintaining a CAP and finally, terminating a CAP. Although the result remains merely a guideline rather than legislation, a purchaser of shares would be well advised to conduct its due diligence of CAPs with a view to ensuring that the CAP sponsor has, in fact, complied with them.

Despite the real issues presented in the investment of CAPs, from a general point of view, it is fair to say that so long as the obligation to contribute has been satisfied, the single most significant obligation of an employer in respect of these arrangements is discharged and they should not be as problematic, in concept, as would be a DB arrangement.

It should be noted that the current level of tax assisted retirement savings permitted under the ITA is, as with DB RPPs, insufficient for high income earners under DC RPPs and, although they remain rare, there is an increase in the number of DC SERPs developing in Canada. As is the case with DB SERPs, it is typical that the DC SERP is not prefunded and, therefore, even in a DC environment there is the possibility that an unfunded liability under a DC SERP will exist. In these unfunded arrangement, it is common to find is a notional accounting of contributions which is maintained along with imputed investment returns. Accordingly, vigilance on the retirement front in these matters is particularly necessary.

For the balance of this paper no further specific mention of DC arrangements will be made, but unfunded DC SERPs should be considered to present issues which are virtually identical to those found in respect of unfunded DB SERPs.

(e) Special Concerns for Unionised Workforces

There may be significant issues to be dealt with in certain corporate re-organisations when operating in a unionised environment. Accordingly, the first order of business in dealing with benefit plans in a unionised environment is to determine whether the programs are "bargained" or not. It is beyond the scope of this paper to provide an analysis of those complicated issues, but suffice it to say that it is a matter of law and significant jurisprudence as to whether or not a program will be viewed at law as being bargained. To the extent it is the subject of collective bargaining, it will typically be impossible under the terms of the collective agreement for the employer to unilaterally amend the program. This may not preclude changes in the identity of the actuary who determines the contribution amounts, but would preclude changes in the terms of the plan. Accordingly, it is important to determine whether the benefits program is circumscribed by a collective bargaining agreement or not.

A secondary issue which may arise, is the assertion by the bargaining agent that it is impossible to divide the bargaining unit between retirees and active employees. That is, in an asset purchase context the bargaining agent may grieve against the purchaser the fact that the business transaction contemplates that the pension liabilities for the retired employees formerly employed in the bargaining unit remain with the vendor while the liabilities for the active employees are transferred to the purchaser and its pension plan. The bargaining agent would be concerned that it would no longer be in a position of leverage to attempt to obtain *ad hoc* increases to retirees'

pensions if the vendor retains responsibility for those retirees. In short, the threat of a strike against the purchaser will do little to motivate the vendor to provide *ad hoc* pension increases to the retirees. It is does not seem likely that the bargaining agents' view in this context would prevail. However, this should serve as a warning to those involved in mergers and acquisitions work that the bargaining agent may from time to time try and take such a position.

Part II – Mergers & Acquisitions

1. Share Purchase or Sale Transactions

The first specific form of corporate reorganisation to be considered in this paper will be the share purchase or sale. The basic context is fairly simple from a human resources' perspective in that the sale or purchase of the shares does not affect the employment relationship – with the possible sole exception should any change of control provisions exist in the target corporation's benefits programs. All that needs to be done in the context of this type of transaction is to ensure that the *status quo* is maintained and that the sources of all liabilities have been reasonably ascertained so that each party understands what liabilities exist with respect to benefits programs in the target corporation. The following will consider these issues from the perspective of the vendor first and then the purchaser.

(a) Vendor's Perspective

While in some cases vendors will prefer to act in a reactive manner to concerns a purchaser may raise as the purchaser conducts its due diligence, some vendors take a proactive approach and want to understand all of the benefits issues prior to or at least coincident with the purchaser uncovering the issues. Vendors will be asked to provide substantial representations and

warranties with respect to benefits plans and the persons bound by the representations will need to have comfort that the representations can be given or, if not, how to describe the exceptions to the requests. Accordingly, it is becoming more and more common for vendors to undertake their own level of due diligence in order to determine, in advance of the purchaser, the potential problems that may exist and be discovered by purchasers so that, in responding to the purchasers' concerns, they have a high level of awareness and have had opportunity to plan an explanation or even adopt a course of action in anticipation of these specific requests. The first level of diligence is to identify all relevant plans (including those which have no current accruals) and then to determine the liabilities and the assets backing the benefits promises so as to assess whether there are unfunded liabilities, their quantum and how they should be dealt with.

(i) Target Participates in Corporate Group Plans

One special but not uncommon set of circumstances which can require a different approach in the benefits area of a transaction arises when the target corporation is part of a larger corporate group and is not the sole employer participating in various benefits programs including pension plans. In the event that the target corporation is simply one corporation among many participating in a registered pension plan or a SERP, the transaction will be completed, from a benefits' perspective, more like an asset purchase than a share purchase. The RPPs and SERPs are likely to need to be split up amongst the "retained" and departing corporations in the group and a decision will have to be made as to whether the existing arrangements remain with the target or whether the target is required to (a) establish its own separate RPP and/or SERP and (b) assume liabilities for its employees by means of some form of asset and liability transfer. Such a circumstance will likely present an issue as to whether or not the liabilities for the former employees of the target corporation (or, in some cases, the business which it operates, in the

event that the business was previously operated as a division and has been recently spun off to the target corporation) should remain with the corporate group or be transferred to the target's plan. This issue will be dealt with in the same manner as an asset purchase and reference to may be made later in this paper. In connection with a pension asset and liability transfer, the vendor may wish to cause the pension plan restructuring to occur, or at least be effective, prior to the time the sale is pursued by re-organising the pension arrangements before offering the corporation for sale. In this way, while the purchaser can complain over the methodology of the transfers there will be no need to negotiate that element which can be complex and time consuming.

(ii) Search for Unfunded Liabilities

Issues of both a basic and an esoteric character may emerge in the course of a due diligence review of the target's benefits arrangements. It is important that a vendor identify supplementary pension plans as these are typically unfunded or at least underfunded and every purchaser will be focussed on them. A review of the funded status of the registered pension plans should be conducted to determine the same and may reveal whether there is opportunity to enhance the purchase price to reflect a surplus. In the context of a share sale which merits a fair amount of vendor's diligence, the vendor may wish to review its pension fund arrangements to ensure that the investments held thereby are all permitted investments. Moreover, to the extent that more exotic derivative transactions (including SWAPs) have been entered into, the vendor may wish to ensure that the counterparties are properly bound so that the purchaser will not raise concerns of potential exposure under invalid or unenforceable contracts. More routinely, the vendor should check to confirm that the foreign property limits in a registered pension plan have been

observed.[14] Of course, the existence of post-employment indexation features (whether contractual provisions or as a result of a consistent past practice of *ad hoc* increases that may be deemed to give rise to a promise in either RPPs or SERPs) should be reviewed as these may be the sources of potential future liabilities. Other potential sources of future liabilities include improper allocation or distribution of surplus and expenses improperly charged to the plans.

Finally, the existence and operation of any change of control provisions should be well understood by a vendor before the purchaser begins to question these particular features.

(b) Purchaser's Perspective

The purchaser's perspective is different from the vendor's perspective in that the vendor simply wishes to ascertain what issues may arise in the context of a share purchase transaction and to be comfortable that it is positioned to give the representations requested of it. On the other hand, the purchaser is vitally interested in uncovering all of the potential unfunded liabilities or other sources of large liability in order to properly price the transaction or, in the extreme case, whether to proceed with the transaction. To do so, the purchaser will seek detailed representations and warranties in respect of the benefits plans. A sample of these kinds of representations and warranties is set out below:

- all of the Benefit Plans are listed in Schedule • and the Vendor has delivered to the Purchaser true, complete and up-to-date copies thereof and all amendments thereto together with, as applicable, all funding agreements, all summary descriptions of the Benefit Plans provided to past or present participants therein, the most recent actuarial reports, the financial statements, if any, and evidence of any registration in respect thereof;

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[14] This make no longer be required if the proposal in the 2005 Federal Budged to eliminate the foreign property rule effective for 2005 and later taxation years is implemented.

- no promises or commitments have been made by the Vendor or the Corporation to amend any Benefit Plan or to provide increased benefits thereunder to any employee, except as required by applicable legislation;

- all of the Benefit Plans are, and have been since their establishment, duly registered where required by legislation (including registration with the relevant tax authorities where such registration is required to qualify for tax exemption or other beneficial tax status) and are in good standing under, and in compliance with, their terms, all applicable legislation and administrative guidelines issued by the regulatory authorities;

- all employer or employee payments, contributions and premiums required to be remitted, paid to or in respect of each Benefit Plan have been paid or remitted in a timely fashion in accordance with the terms thereof and all applicable legislation, and no taxes, penalties or fees are owing or exigible under any Benefit Plan;

- except as permitted by the Benefit Plans and applicable legislation, there has been no withdrawal of surplus assets or any other amounts from any of the Benefit Plans other than proper payments of benefits to eligible beneficiaries, refunds of over-contributions to plan members and permitted payments of reasonable expenses incurred by or in respect of such Benefit Plan;

- all employer contribution holidays have been permitted by the terms of the Benefit Plans and have been in accordance with applicable legislation;

- there are no material actions, suits, claims, trials, demands, investigations, arbitrations or other proceedings pending or, to the knowledge of the Vendor threatened with respect to the Benefit Plans against the Corporation, the funding agent, the insurers or the fund of such Benefit Plans;

- neither the execution, delivery or performance of this Agreement, nor the consummation of any of the other transactions contemplated by this Agreement, will result in any bonus, golden parachute, severance or other payment or obligation to any current or former employee or director of any of the Vendor (whether or not under any Benefit Plan), or materially increase the benefits payable or

provided under any Benefit Plan, or result in any acceleration of the time of payment or vesting of any such benefits;

- none of the Benefit Plans require or permit a retroactive increase in premiums or payments, and the level of insurance reserves, if any, under any insured Benefit Plan is reasonable and sufficient to provide for all incurred but unreported claims;

- except as permitted by the Benefits Plans, their applicable funding agreements and applicable funding agreements and applicable legislation, there has been no withdrawal of assets or any other amounts from any of the Benefits Plans other than proper payments to eligible beneficiaries, refunds of over-contributions to plan members and permitted payments of reasonable expenses incurred by or in respect of such Benefit Plans;

- no order has been made or notice given pursuant to any applicable legislation requiring (or proposing to require) the Corporation to take (or refrain from taking) any action in respect of any Benefit Plan, and no event has occurred and no condition or circumstances exists that has resulted or, could reasonable result, in any Benefit Plan (i) being order or required to be terminated or wound-up in whole or in part, (ii) have its registration under any applicable legislation refused or revoked, (iii) being placed under the administration of any trustee or any regulatory authority or (iv) being required to pay any material taxes or penalties under any applicable legislation;

- the Corporation has no obligation in respect of any Benefit Plans that are multi-employer pension plans or multi-employer benefit plans except contribution obligations as set out in the collective agreements provided to the Purchaser.

It should be noted that a number of these representations are difficult for a vendor to give. Therefore, the purchaser may have to undertake significant diligence to "satisfy itself" in the event that it wishes to complete the transaction without some significant representations. Alternatively, the purchaser may seek in place of such representations some form of indemnity. That being said, a purchaser may be unable to complete a transaction unless it is provided with

either (a) key representations against which it may seek indemnity should the representation prove to be incorrect or (b) a sufficiently broad indemnity. In many cases, it will be impossible to undertake the very precise detailed review necessary to uncover all potential problems. If satisfactory representations cannot be obtained, at a minimum the purchaser may seek a representation that all material documents pertaining to the benefits plans have been provided to it, so that if something that may have disclosed a problem is omitted, there may be an opportunity to pursue a breach of warranty on this basis. The parties should understand that with respect to RPPs and SERPs, the time commitments are so far out in the future that issues will often not emerge for several years. Accordingly, purchasers are advised to attempt to negotiate lengthy survival periods for the benefits representations.

2. Corporate Amalgamations

When a group of corporations are in the process of trying to streamline structure by means of an amalgamation, this often means that the employee benefits plan structure is also intended to be the subject of some streamlining. There is often thought of merging plans and, in particular, RPPs.

In addition to concerns with respect to collectively bargained retirement plans, there will be various administrative issues to consider. To the extent that the amalgamating corporations each have separate RPPs and SERPs, even if the plans are not to be merged, each RPP and SERP will have to be amended so as to ensure that the employees of the amalgamated corporation do not have the right to participate in both plans.

The unintentional triggering of a change of control provision in a SERP by a corporate re-organisation is not uncommon. In these circumstances it may be necessary to obtain waivers or

consents from the SERP members to avoid having to fund the arrangement or call a letter of credit. Often, due to the internal nature of the event, the operation of the provision in the context is discovered late in the process and may cause embarrassment and even serious problems. Accordingly, early awareness of these provisions and, better yet, thoughtful design of the change of control feature when it is adopted is desirable.

Should it ultimately be decided that the SERPs and RPPs should be merged, some of the recent case law (namely the *Transamerica*[15] and *Baxter*[16] decisions) in connection with mergers of RPPs the assets of which are held in trust as well as certain regulatory responses (i.e. FSCO's "moratorium" on mergers and asset transfers) should be kept in mind. The remainder of this section of the paper is devoted to a discussion of these issues.

Transamerica[17]

(a) The Facts

The facts of *Transamerica* are, briefly, as follows. Following the amalgamation of NN Life Insurance Company of Canada ("NN") and Halifax Life Insurance Company of Canada ("Halifax") to form NN Life Insurance Company of Canada ("Amalgamated NN"), NN's and Halifax's defined benefit pension plans were merged. The Pension Commission of Ontario ("PCO") approved the merger on the condition that the assets and liabilities from the Halifax plan trust (the "Halifax Fund") be kept separate from the NN plan trust and liabilities.

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15 *Aegon Canada Inc. and Transamerica Life Canada v. ING Canada Inc.*, [2004] S.C.C.A. No. 50 leave to appeal to S.C.C. refused on appeal from (2003) 38 C.C.P.B. 1 (Ont. C.A.), affirm (2003) 36 C.C.P.B. 161 (Ont. S.C.J.).

16 *Baxter v. Ontario (Superintendent of Financial Services)* [2004] O.J. 4909 (S.C.J.).

17 This subsection of this paper is extracted from and represents a reworking of "More on Pension Plan Mergers From the British Columbia and Ontario Courts of Appeal" Vol. VII, No. 4 "Taxation of Executive Compensation and Retirement, p. 441, written by my colleague Lorraine Allard.

Notwithstanding this segregation, Amalgamated NN treated the assets of both trusts as a single fund and took contribution holidays based on the surplus in the Halifax Fund.

A few years later, the shares of Amalgamated NN were sold by ING Canada Inc. (the "Vendor") to Aegon Canada Inc. and Transamerica Life Canada (the "Purchasers") who claimed that the Vendor had breached the warranty in the share purchase agreement that all required contributions had been made to Amalgamated NN's pension plan.

(b) The Submissions

The Purchasers submitted that the Halifax Fund assets were only available to pay the pension obligations of the "Halifax employees" (i.e., active and inactive members of the Halifax plan at the time of amalgamation) and could not be taken into account in determining the employer's obligations in respect of anyone who was not a "Halifax employee".

The Vendor submitted that the contribution holiday had no impact on the Halifax employees and that taking the Halifax Fund into account in determining the level of employer contributions to be made to the merged plan did not constitute a breach of the Halifax plan trust.

The lower court agreed with the Purchasers.

(c) The Decision

The Court of Appeal upheld the lower court decision. It found that "the clear terms of the Halifax Trust precluded any part of the capital or income of the fund from being diverted to any purpose other than the exclusive benefit of the beneficiaries of the Halifax Trust" and that Amalgamated NN was obliged "by the terms of the Halifax Trust and by the terms of the

undertaking it gave to the PCO to maintain the assets of the Halifax Trust separate and apart from the other assets and liabilities" of the Amalgamated NN's pension plan [par. 7]. It rejected the Vendor's argument based on *Air Products*, holding that the lack of present entitlement of the Halifax employees to surplus did not justify the use of that surplus by Amalgamated NN for a purpose contrary to the terms of the trust.

What is most problematic for future (and potentially past) pension plan mergers in Ontario is the Court of Appeal's dismissal of Justice Grange's comments in *Heilig v. Dominion Securities Pitfield Ltd.* ("Heilig").[18]. In that decision, two companies, each of which sponsored a defined benefit pension plan, amalgamated. The amalgamated company withdrew surplus from one of the plan funds and merged the two plans effective as of the date of the corporate amalgamation. The members of the pension plan from which surplus had been withdrawn brought an application for a declaration that the plan in surplus had been terminated as of the date of the amalgamation and an order directing that the amalgamated company repay the withdrawn surplus with interest (which the amalgamated company undertook to do before the hearing of the application). The members were successful at trial but lost on appeal.

In rejecting the notion that a plan merger effects a termination of the plan, Justice Grange stated in *Heilig* that:

> I see no reason why the two pension plans of merging companies cannot be merged into one continuing plan just as the two companies amalgamate into one continuing company. Certainly, there can be no loss of benefit for the beneficiaries of either plan without their consent. But that does not happen in the merger of plans such as that in the case at bar. It makes no difference that one plan may be in surplus and the other not. There is no obligation for an employer contribution until actuarial figures require it. The merger is not unlike the situation resulting from an expansion of the company staff and a large influx of new members to the plan. [pp. 399, 400.]

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18 (1989), 59 D.L.R. (4th) 394 (Ont. C.A.).

The Court of Appeal in *Transamerica* held that *Heilig* posed a very different issue and that Justice Grange was not addressing the question at bar. His comments, which were *obiter*, were found to be of no assistance.

FSCO's "Moratorium" on Mergers and Asset Transfers[19]

FSCO reacted to *Transamerica* by adopting its policy regarding the inter-plan transfer of assets. This policy provides that a transfer of assets on sale or merger may be favourably considered by the Superintendent only in specified situations:

> (i) where the plans have no defined benefit component or are not subject to a trust,
>
> (ii) the receiving plan undertakes to maintain the transferred assets separate and apart, the terms of the transferring plan(s) and trust(s) do not prohibit the transfer and the surplus entitlement language is consistent under the receiving and transferring plans, or
>
> (iii) a court of competent jurisdiction has determined that the transfer of assets is legal and binding and all rights of appeal have been exhausted.

Where the transfer is on a sale, the parties have an additional avenue which is to transfer the assets to a newly established plan where the transfer does not breach the terms of the original plan and trust, a proportionate share of surplus (if any exists at the time) is also transferred (unless the employer clearly owns the surplus in the original plan and the entitlement is demonstrated in the application), and the surplus entitlement language is consistent under the original and newly established plans. If the merger does not fit into one of these situations, it will be "considered on a case-by-case basis" if "it can be differentiated from the *Transamerica* decision".

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19 This subsection of this paper is extracted from a yet to be published paper, written by my colleague Lorraine Allard.

This is, obviously, a very unsatisfactory state of affairs. In the context of sales of businesses, it could lead to a proliferation of plans since purchasers are unable to have defined benefit pension plan assets and liabilities associated with newly acquired employees transferred from trusteed pension plans to a pre-existing pension plans.

Baxter[20]

Baxter was released on December 1, 2004. Although this decision sheds further light on the developing area of pension plan mergers, a recent settlement in the case means that the Court of Appeal will not be given an opportunity to shed even more light.[21]

(a) The Background

Effective June 30, 1952, National Steel Car Corporation Limited ("NSCC"), the predecessor of National Steel Car Limited ("NSC"), established the National Steel Car Corporation Limited Pension Plan (the "Original Plan"). The Original Plan covered both salaried and hourly employees. It was funded through a group annuity policy between NSCC and the Mutual Life Assurance Company of Canada and annuity contracts with the Canadian government Annuities Branch and, after June 30, 1964, through a deposit administration annuity policy provided by the Mutual Life Assurance Company of Canada.

Effective July 1, 1965, the Original Plan was split into a pension plan for salaried hourly-paid employees of NSCC (the "Salaried Plan") and a pension plan for hourly-paid employees of NSCC (the "Hourly Plan").

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20 This subsection of the paper is almost entirely based on and represents a reworking of a yet to be published paper written by my colleague Lorraine Allard.

21 Leave to appeal to the Court of Appeal of Ontario had been granted on December 16, 2004.

On July 18, 1994, the funding arrangements for the Salaried Plan and the Hourly Plan were changed to a pension trust agreement between NSC and the Canada Trust Company (the "Trust Agreement").

On January 20, 2000, NSC advised the members, former members, and retirees of the Salaried Plan and the Hourly Plan that it had decided to merge the two Plans retroactively to March 1, 1999. The notice stated that the merger would not affect the pension benefits earned to date in any way, nor would it affect the way in which benefits would be earned in the future.

On February 2, 2000, an application to transfer the Salaried Plan assets to the Hourly Plan was filed with the Superintendent. In the application, the employer certified that the funding excess remaining in the merged plan immediately after the transfer was such that the funding requirements for the merged plan could be met using these surplus assets.

On November 20, 2000, the Superintendent invited the employer, the appellants (representatives of certain members and former members of the Salaried Plan), and the United Steelworkers of America to make submissions to the Superintendent on the asset transfer.

In a letter dated March 2, 2001, the Superintendent consented to the transfer of assets of the Salaried Plan to the Hourly Plan.

(b) Plan Provisions

Section 17.1 of the Original Plan expressly permitted mergers:

> The Company intends to maintain the plan indefinitely but necessarily reserves the sole right to amend, suspend, segregate, merge or terminate the plan and to change the method of [sic] medium of funding the plan benefits, all as the company may in its absolute discretion, determine. [par. 2] [Emphasis added.]

The 1965 and 1966 versions of the Salaried Plan also expressly granted the right to merge the Salaried Plan.

Effective January 1, 1972, section 18.4 of the Salaried Plan was amended to state:

> Should the Plan be terminated, the Company shall not be obligated to make any further contributions to the Plan and the assets thereunder shall be allocated for the provision of the accrued benefits to which members of the Plan, Pensioners, their estates, designated beneficiaries and joint annuitants are entitled in such equitable manner as may be determined by the Company in consultation with the actuary. Such benefits shall be provided in the form elected by Members under the terms of the Plan. Should a surplus remain under the Plan after the provision of all accrued benefits to Members of the Plan, Pensioners, their estates, designated beneficiaries and joint annuitants, such excess funds shall revert to the company. [par. 4] [Emphasis added.]

(c) Tribunal Decision

The appellants requested a hearing under s. 89 of the OPBA with respect to the Superintendent's decision. A majority of the Financial Services Tribunal (the "Tribunal") determined that it did not have jurisdiction to conduct a hearing but the full Tribunal agreed to proceed to consider the merits of the applicants' case in the event the Tribunal was wrong in its conclusion as to jurisdiction. The Tribunal unanimously rejected the appellants' arguments.

(d) The Submissions

The appellants argued before the Ontario Divisional Court (the "Court") that the 1966 version of the Salaried Plan had the effect of establishing a trust in respect of the Plan assets for the benefit of the members of the Plan. They also maintained that the transfer of assets did not protect "other benefits" of the members of the Salaried Plan as required by subsection 81(5) of the OPBA, which reads as follows:

> The Superintendent shall refuse to consent to a transfer of assets that does not protect the pension benefits and any other benefits of the members and former members of the original pension plan or that does not meet the prescribed requirements and qualifications.

They submitted that the Tribunal had erred in finding that a pension plan member's interest in surplus is contingent upon termination of the plan and the existence of an actual surplus at that time, and does not fall within the expression of "other benefits" of the members in s. 81(5) of the OPBA.

The appellants also argued that, (i) pursuant to section 81(5), the contributions to the Salaried Plan could not be used in the merged Plan for the benefit of the Hourly Plan because the Salaried Plan members would lose the protection those assets provided for the long-term solvency of the Salaried Plan and that (ii) "other benefits" consisted of the exclusive rights to all the benefits of the contributions to the Salaried Plan and the funding protection built into the Salaried Plan.

The respondents (the Superintendent, NSC and the United Steelworkers of America) argued before the Court that the merger adequately protected the "pension benefits" of the members as defined under the PBA. In a defined benefit plan, the pension promise consists of the promise that the members will receive the benefits as defined under the plan, regardless of the investment performance of the plan fund. The Superintendent had determined that the pension promise was adequately protected by applying FSCO policy A700-251 which requires that the merged plan have sufficient assets to pay all benefits set out in the plan as at the date of merger. The policy contrasts with ordinary course funding of defined benefit plans which may be less than fully funded at any given time, subject to the employer's obligation to make special payments to return the plan to fully funded status.

The respondents submitted that the appellants' claim to an interest in the plan's assets, over and above the assets required to fully fund the pension promise constituted a claim to the actuarial

surplus. Pursuant to the Supreme Court of Canada's decision in *Air Products*, even when a pension plan takes the form of a trust, employees cannot claim surplus in an on-going plan.

(e) The Decision

After finding that the Tribunal did have jurisdiction to hear the matter, the Court agreed with the respondents that the appellants' request amounted to a claim on surplus:

> The appellants' argument that contributions made to the salary plan are an "other benefit" under s. 81(5) of the PBA imports a defined contribution concept into a defined benefit plan. It implies that the Salaried Plan members have some guarantee respecting the contributions, in addition to the guaranteed defined benefit. In our view, and we agree with the Superintendent, this concept is inconsistent with the very definition of a defined benefit pension plan. In reality, the appellants' claim as to "other benefits" is really a claim to the actuarial surplus. Surplus is neither a pension benefit, nor an "other benefit" under the PBA. Until the right to surplus crystallizes - and the right to surplus does not crystallize upon a transfer of assets - the surplus is simply as expressed in Schmidt, supra, "the excess of the value of the assets of a pension fund related to a pension plan over the value of the liabilities under the pension plan". [par. 65]

The Court then proceeded to examine the relevant provisions of the OPBA. It disagreed with the appellants that the term "other benefits" in subsection 81(5) includes surplus. It held that since the only types of benefits defined in the OPBA other than "pension benefit" are "bridging benefits" and "ancillary benefits", and since neither of these benefits include pension fund surplus assets, the term "other benefits" can only mean benefits that are provided by a pension plan that are not pension benefits or ancillary benefits as defined in the OPBA:

> If the appellants are correct that "other benefits" includes surplus, then an employer would be required to fund a pension fund to maintain the current level of actuarial surplus in the pension plan, a result which in our view is contrary to the specific funding regime set out in the PBA and regulations (see s. 55(1)). [par. 66]

It also held that section 81 of the OPBA does not provide any right to a distribution of surplus upon a plan merger:

> In fact, there is an express statement in s. 81(1) that the original pension plan is deemed not to be wound up and that the new plan is deemed to be a continuation of the original plan. Hence, any surplus that is

> transferred on a merger is not withdrawn, but remains in the plan. This, in our view, is consistent with the reasoning of the Supreme Court of Canada in Schmidt, supra, and indeed is consistent with the regime under the PBA. Surplus is not payable upon retirement or termination of employment or membership in a pension plan. While the plan is continuing, surplus may only be withdrawn from the plan upon the employer's application and with the consent of all the members. [par. 67]

The Court then turned to the applicable jurisprudence and, more specifically, to the Ontario Court of Appeal's decision in *Transamerica* and the Court of Appeal of British Columbia's decision in *Buschau v. Rogers Cable Systems Inc.*, [2001] B.C.J. No. 50 (C.A.) ("*Buschau*"). It concluded that "where the terms of a pension plan in trust permit a merger, there is nothing in the general law of trusts that prevents a merger of trust funds", which is "in line with the Ontario Court of Appeal in *Heilig*".[22]

The Court distinguished *Transamerica* based on its finding that the Salaried Plan was not subject to a trust until 1994 at which time the Salaried Plan provided that the employer was entitled to surplus.

> In the case before us, we are not persuaded the appellants have established either that the salary plan was subject to a trust, or that the specific terms of any such trust (if indeed there was one) precludes the merger. To the contrary, at all material times, both merging plans expressly permitted a merger and the merger simply restored the unified plan that was originally established in 1952. [par. 70]

In addition, far from imposing the condition that the trust funds be kept segregated, as had the PCO in *Transamerica*, the Superintendent had approved the asset transfer unconditionally.

The Court distinguished *Buschau* by holding that the Court of Appeal of British Columbia:

> did not hold that the specific terms of the trust preclude a merger, rather, in the specific circumstances of that case, where the fund subject to the trust was closed and the beneficiaries sought to obtain distribution of the trust funds under the rule of Saunders v. Vautier, the beneficiaries were entitled to segregation and an accounting of the assets to which they had established their beneficial entitlement. In other words, the merger proceeded, subject to this segregation and accounting. [par. 72]

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22 *Heilig v. Dominion Securities Pitfield Ltd.* (1989), 67 O.R. (2d) 577 (Ont. C.A.)

With due respect, although the Court of Appeal of British Columbia did not specifically say that the pension trusts in *Buschau* could not be "merged", it is difficult to find any other meaning in its decision that the members of the Premier Plan (one of the pre-merger plans) had the right to invoke the rule in *Saunders v. Vautier* to collapse the Premier Plan trust than that the Premier Plan trust had and could not be merged with the other pension trusts:

> The Plan has long been closed, and the only question is whether the right that belonged to Premier Plan members as a class prior to merger by virtue of the rule in Saunders v. Vautier still exists, or whether that right was diluted (probably to the point of extinction) by the merger down to a right shared with all 4,300 members of the RCI Plan.
>
> In my view, the right of the members of the Premier Plan to invoke Saunders v. Vautier (or for that matter I suppose, the Trust and Settlement Variation Act, R.S.B.C. 1996, c. 463, if applicable) in respect of the Premier trust remains unaffected by the merger, just as their rights to receive the Premier Plan surplus on termination of the Premier trust continues notwithstanding the merger. [par. 67, 68]

These pronouncements follow a discussion of the meaning of the merger of pension plans as opposed to the merger of pension plan trusts in which the Court of Appeal states that "it is difficult indeed to segregate conceptually the Premier Plan from the Premier trust in terms of merger." The implication is that its use of the term "merger" should be read to refer to the merger of the pension plans. The Court of Appeal of British Columbia commented on its decision in *Buschau* in *Bower v. Cominco Limited*,[23] ("*Cominco*") where it stated that:

> As I read Buschau, the court accepted that pension plans and their funds may be merged provided that the terms of the plans and the trusts permit such a union. Where funds are held in accordance with a trust which specifically devotes the corpus of the trust to the exclusive use of the beneficiaries, it follows that the fund may not be used for any other purpose. Merger is not permitted in that case. [par. 74]

(f) The Possible Implications

The facts in *Baxter* were unusual: (i) the Original Plan referred to the possibility of a merger, (ii) the Original Plan was funded through an insurance contract, (iii) the Original Plan was amended

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[23] 2003 BCCA 537.

to provide to the Company ownership of surplus on termination of the Plan while the Plan was still funded through an insurance contract, and (iv) the splitting of the Original Plan into two occurred while it was still funded through an insurance contract. Indeed, short of an explicit right to merger in the original plan documentation, it is difficult to imagine a fact pattern more favourable to the Company where the pension plan assets are held in trust at the time of the merger. Clearly, *Baxter* would not have been considered under one of the listed situations in the policy but could have been considered on a case-by-case basis, (as could most merger applications given that most situations can be distinguished from *Transamerica* by virtue of the unusual undertaking given to the Pension Commission of Ontario by the plan sponsor in that case.)

Baxter does what no merger decision thus far has done – consider the role of statutory law and the regulator in permitting pension plan mergers. Sections 80 (in the context of the sale of a business) and 81 (in all other cases) of the OPBA authorizes the Superintendent to consent to transfers of assets except where the transfer "does not protect the pension benefits and any other benefits". As discussed above, the Court found that pension plan members have no right to a distribution of surplus under those provisions. The issue is really whether the fact that pension plan members have no right to a distribution of surplus under these provisions completely eliminates any right, in all circumstances, which may exist in equity which would impede or even prevent the commingling of pension assets from different trusts. A secondary issue is whether the regulator has the capacity to decide whether any such rights exist and whether the merger is sufficiently protective of those rights.

The Court did not delve into these questions because of the favourable fact pattern in this case. If the common law does not normally allow the merger of pension trusts, except under special

circumstances such as in *Cominco* (where the provisions of the Pension Fund Society were held to "inform the provisions of the trust") or in *Baxter* (where the provisions of the plans provided that they could be merged), then the courts will have to decide whether the commingling of pension assets in a "merger" may be allowed by the regulator outside of these fact patterns, or whether such commingling cannot, by definition, be sufficiently protective of all existing rights. Due to the fact that pension trusts are dynamic and the beneficiaries of pension trusts are determined as a class, it should be possible to add newly acquired employees, who fit within the class of beneficiaries, to a pension plan and have their past and future benefits funded from the pension trust. If this is the case, then there should be no real impediment to merging two pension trusts and the Ontario Court of Appeal's decision in *Heilig* should eventually be recognized as a correct statement of the law in this area.

Given that the appeal in *Baxter* has been abandoned, FSCO will have to decide in the short to mid term what, if any impact, the Court's decision has on its policy regarding the inter-plan transfer of assets and whether such policy should be revised Even if FSCO decides against this, *Baxter* will serve as an example of a situation where FSCO should approve a merger of trusteed plans while still giving consideration to what it believes the Court of Appeal's decision in *Transamerica* means. One can only hope that a new case will come along to further develop this area of the law and give further guidance to pension plan sponsors who struggle to manage these increasingly troublesome benefits.

Other Options

To avoid some of the potential controversy that the merger of DB RPP trusts may cause, other options may be available. One possibility which may be worth exploring is the "wrap around" technique. This would involve amending the overfunded DB RPP to admit to it the members of

the underfunded DB RPP, which may involve broadening the class of beneficiaries, and to ensure that all benefits in respect of these new members will be provided by the overfunded DB RPP's trust less any benefits payable from the trust of the underfunded DB RPP pursuant to the terms of that plan. A concurrent amendment would be made to the underfunded DB RPP so that no future service may be credited thereunder. This technique may or may not eliminate the need to contribute to the underfunded DB RPP but does eliminates future service liabilities and may reduce past service liabilities of such plan but the applicable pension standards legislation should be reviewed to ensure its effectiveness.

3. Asset Purchase and Sale Transactions in Respect of Pension Matters

The treatment of pension matters is merely one subset of the whole employment relationship which must be dealt with under any asset purchase and sale and, therefore, the issues which emerge in the pension context must first be dealt with in concert with the overall "deal" in connection with employment obligations.

(a) Context of Benefits Issues in Asset Sale/Purchase

Typically the purchaser will be required to offer employment to the employees and the issue will be whether that offer of employment must be on terms and conditions which are "identical" to the existing terms and conditions – which may be required as a result of collective bargaining agreements – or whether there is latitude for differences in the programs to be provided by the purchaser. A second issue, and the one which has perhaps the greatest impact on the pension treatment in such a transaction, is to what extent, if any, the past service benefits rights of the employees will be honoured by the purchaser.

(b) Registered Pension Plans

Because RPPs are prefunded, the decision to assume past service liabilities is a critical one because this is normally accompanied by a transfer of the assets already allocated in respect of the transferring employees. Past service obligations are not really a major concern in connection with DC pension arrangements but are a real issue with respect to DB programs, particularly because the employees often will be adversely affected if past service is not recognised.

The range of options for dealing with RPPs is as follows:

- Purchaser provides no DB RPP.
- Purchaser provides a DB RPP but does not recognise past service and there is no asset transfer.
- Purchaser provides a DB RPP and recognises past service but there is no asset transfer.
- Purchaser provides a DB RPP, recognises past service and there is a transfer of assets.

Returning to the past service issue, even in a simple flat benefit plan for a collectively bargained workforce this can be important to the employee. For example, if the flat benefit level is $40.00 per year of service on the date of sale but might rise to $60.00 per year of service at the end of 20 years when the employee retires, whether all years of service or only post-closing years of service are recognised by the purchaser can yield a significant difference in the employee's benefit. A numerical example may illustrate this:

- John Doe has 10 years of service with the vendor pre-closing and 20 years of service with the purchaser post-closing.

- If all 30 years of service are considered at the $60.00 level, then the employee's monthly benefit would be $1,800.00.

- However, if past service with the vendor is not recognised under the purchaser's plan (which may raise its own collective bargaining issues), and the responsibility for the past service benefit remains with the vendors, the total benefit will be the aggregate of the amount payable from each of the vendor's and the purchaser's pension plans as follows:

  Vendor's Plan - 10 years times $40 equals $400.00/ month plus

  Purchaser's plan 20 years multiplied by 60 equals $1,200.00/month

  Total equals $1,600.00/month.

- Thus our fictional employee would lose out to the extent of $200.00 per month as a result of the non-recognition of the past-service under the purchaser's pension plan.

Assuming the RPP is bargained, either the purchaser will recognise the past service but not insist upon a transfer of assets from the vendor's plan (and thus would bear a total obligation of $1,400.00 per month to satisfy our fictitious employee instead of only $1,200.00 in the pro rated example and has to do so without the benefit of the assets already contributed to the vendor's plan in respect of the employee) or it will insist upon an asset and past service liability transfer.

Once an asset transfer is decided upon then the "fun" begins. The vendor and the purchaser will have to negotiate the actuarial basis for the transfer, taking cognizance of the pension standards regulators guidelines that are issued from time to time, and may also have to deal with the thorny issue of surplus. These are various approaches to valuing asset transfers. One method is simply to provide that the assets to be transferred will equal the liabilities. However, there are two broad bases to measure liabilities and different methods and assumptions may be adopted too. If the plan is precisely fully funded and the parties can agree on the basis then this should not be a problem. But if the vendor's plan is grossly underfunded then the regulators may only consent to the transfer if the vendor makes a special contribution to its plan prior to completing the asset transfer so that the remaining plan members are not adversely affected by the transfer (i.e. their benefits should not be less well funded after the transfer is made). If the plan is overfunded then the regulator may first question why a share of the surplus is not being transferred (and if it is not then query whether the employees are to be given an interest in any subsequent surplus sharing from the vendor's plan, despite the asset transfer). Another transfer basis that may be approved by regulators is to provide that the transfer will be based on the funded ratio of the pension plan so that if that ratio is 110% then an amount equal to 110% of the assumed liabilities is transferred and similarly if it is 80% then an amount equal to 80% of the assumed liabilities is transferred. The latter is considered fair because the funded status of the employees and others remaining in the vendor's plan remains the same and the ratio for the transferring employees also remains the same.

Finally, of course, if surplus is transferred then there will be the issue as to how much and how much it is worth. Because surplus is transient, based on investment performance and actuarial

assumptions, and it may really only be useful for contribution holidays, a purchaser will rarely pay dollar for dollar for surplus.

(c) SERPs

The treatment of supplementary pension arrangements may be a precise parallel of the registered pension benefits – particularly since the ITA provisions concerning RCAs now provide for interplan asset transfers.[24] However, few if any RPPs contain change of control provisions while many SERPs contain such features. Accordingly, the existence and effect of any such provision must be established.

Part III – Restructuring in Insolvency

1. Background

(a) Technical Aspects of Pensions Law in Insolvency

In the context of insolvency proceedings, pension plan related issues which demand time and attention are generally restricted to DB RPPs, although there could also be some implications for SERPs. The main issues relate to dealing with significant deficits as well as cash flow problems associated with funding DB RPPs. Essentially a DB RPP represents a promise to pay a certain benefit at a future point in time. As discussed in Part I of this paper, the amount of the benefit is determined by reference to a specified benefit formula or a percentage of earnings.

It must be appreciated that there are various types of employer pension contributions – in general terms, these will often relate to (a) the actuarial basis for the determination of plan liabilities, and

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[24] See subsection 207.6(7) of the ITA.

(b) whether the contributions related to "past service" (to fund deficiencies in respect of past pension obligations and often referred to as "special payments") or current service (to fund obligations for the current period). The following discussion is a simplified description of very complex actuarial and statutory issues. Expert actuarial advice should be obtained to explore the details and nuances of these issues. With respect to the actuarial basis, the DB RPP will be valued both as if the plan and the corporation is ongoing ("a going concern basis") and as if the plan is terminated (giving rise to a solvency valuation or wind up valuation; the term solvency will be used herein) – with different actuarial methods and assumption prescribed or customary for the different bases. Currently, a solvency valuation gives rise to greater liabilities in most pension plans than does an ongoing valuation and so solvency funding gives rise to greater periodic contributions.

The employer's contribution amount to fund a DB RPP is determined by an actuarial report. The actuarial report will determine the current funded status of DB RPP and estimate the necessary level of contributions to meet any current service and past service obligations on each of a going concern and solvency basis. Any funding deficiency identified in the actuarial report is amortized over a prescribed period (five years on a solvency funding basis and fifteen years on a going concern basis). Generally, pension legislation requires actuarial reports to be filed on a triennial basis and the actuarial reports are "good" for the duration of that period, but in some instances more frequent updating of the actuarial report is required[25] or undertaken on a voluntary basis. Regardless, the administrator must file the report within nine months of the

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25 When an actuarial report indicates "solvency concerns" (under section 14 of the regulations to the OPBA, a report will indicate solvency concerns where the ratio of the solvency assets to the solvency liabilities is less than 0.8 or the solvency liabilities exceed the solvency assets by more than $5,000,000 and the ratio of the solvency assets to the solvency liabilities is less than 0.9) the next actuarial report must be prepared (and certified with a valuation date) within one year.

valuation date (which usually results in the filing of the report by September 30 since actuarial reports are typically prepared on a calendar basis). Until the new actuarial report is filed, the amount of the contributions will continue based on the "old" valuation report. Depending upon any number of relevant factors, the contributions actually required for a period will be greater or lesser under the new valuation than under the old valuation. Where the contributions increase under the new report, within 60 days of the filing of the report, the difference between the amounts actually contributed and those called under the new report must be remitted. This can often be in the millions or tens of millions of dollars and so when cash reserves are limited attention to this possibility is required.[26]

In Ontario, contributions are to be remitted monthly (quarterly, under federal pension legislation) in arrears. When an actuarial report indicates that the plan is in a surplus position the employer may be permitted, subject to the language of the relevant plan and trust documents, to take a "contribution holiday" whereby the actuarial surplus is used to fund the employer's current service obligations.

(b) Deemed Trust and Statutory Lien

In Ontario, certain deemed trusts are created under the OPBA[27] in favour of the plan beneficiaries with respect to:

- source-deducted employee contributions until the money is paid into the pension fund;

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[26] As will be illustrated below, the frequency or timing of reports and the rule that calls for "make up contributions (OPBR s. 12) can play a role in seeking court orders to delay filing of these reports.

[27] See subsection 57.

- employer contributions which are due, but which have not yet been remitted; and
- where a plan is wound up in whole or in part, an amount equal to the contributions which have accrued to the date of the wind up, but are not yet due (commonly referred to as "stub period" contributions).

The administrator of the pension plan is also provided with a lien and charge on the assets of the employer, in an amount equal to the deemed trusts.[28]

The deemed trust and statutory lien under the OPBA are enforceable against the employer outside of insolvency proceedings and may adversely affect the priority status of preferred creditors. For example, under the *Personal Property Security Act*,[29] a security interest in an account receivable or inventory is generally subordinate to the interest of a person who is a beneficiary of a deemed trust under the OPBA. Although the law is not clearly and absolutely settled, I believe the conventional thinking surrounding these OPBA deemed trust and statutory liens is that, in the context of proceedings under both the *Companies' Creditors Arrangement Act*[30] (the "CCAA") and the *Bankruptcy and Insolvency Act*[31] (the "BIA"), the statutory lien of the administrator remains enforceable. The deemed trust, by way of contrast, remains enforceable when a company attempts to restructure under the CCAA, but is conventionally considered to be unenforceable in proceedings under the BIA.[32]

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28 See subsection 57(5) of the OPBA.

29 R.S.O., c. P.10. See subsection 30(7).

30 R.S. 1985, c. C-36.

31 R.S. 1985, c. B-3.

32 See generally *British Columbia v. Henfrey Samson Belair Ltd.*, [1989] 2 S.C.R. 24.

Of particular note to secured creditors will be the fact that the courts have determined that the deemed trust created under the OPBA does not extend to the unfunded pension liability upon wind up of the plan, but is limited to the outstanding unremitted contributions that are past due plus those arising in respect of the stub period.[33] Accordingly while the entirety of the pension fund shortfall remains an obligation of the employer, and an obligation exists under the OPBA to fund this deficiency over a period not exceeding five years from the date of windup[34], at present this is an unsecured claim on the assets of the debtor.

Despite the foregoing, a private members bill, Bill C-281[35], could turn the priority of secured creditors on its head by establishing a super priority status for outstanding employee claims, including pension benefits. First introduced in November 2004, Bill C-281 was debated at second reading in December 2004, although currently, the progress of the bill appears to have stalled. In its current form Bill C-281 would establish priority status for all pension funding shortfalls in bankruptcy proceedings by amending the BIA[36] to provide workers with first priority to the proceeds realized from the property of the bankrupt with respect to wages/salaries, severance/termination pay and unfunded pension liabilities. These amounts would be deemed to be a first charge on every realizable asset of the bankrupt, despite any security taken or granted to any other person. Furthermore, the bankruptcy trustee would be required to make any payments owed by the bankrupt to a pension plan so as to eliminate all unfunded liabilities of the plan and allow the pension plan to immediately satisfy all of its obligations to every member of

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33 *Toronto-Dominion Bank v. Usarco Ltd.* (1991), 42 E.TR. 235 (Ont. S.C.J.).

34 See s. 75 of the OPBA and s. 31 of the OPBR. Note that since s. 31 calls for annual funding in advance, this is really a four year period.

35 An Act to amend the Bankruptcy and Insolvency Act, Canada Business Corporations Act, Employment Insurance Act and Employment Insurance Regulations Amendments.

36 The change in priority status would be reflected in paragraph 60(1.3)(a) and section 136 of the BIA.

the plan. Unless the bankruptcy proposal provided for payment of these benefits immediately upon its approval, the bankruptcy judge would not be permitted to approve the proposal.

While the future of Bill C-281 remains uncertain, it has been championed and would obviously be welcomed by plan members as protection of their pension benefits. On the other hand, sources of financing for companies with one or more significant DB RPPs may be restricted and even dissipate entirely where there is a significant risk of an underfunded plan as secured lenders seek to manage the new risk that would exist vis-à-vis unfunded pension liabilities.

It should be noted that Bill C-281 makes no reference to proceedings under the CCAA, therefore, leading to the presumption that the deemed trust and statutory lien analysis would continue to apply.

(c) Pension Benefits Guarantee Fund

The Pension Benefits Guarantee Fund ("PBGF") was established in 1980 to guarantee the payment of certain pension benefits,[37] in respect of employment in Ontario, upon the full or partial wind up of a qualifying[38] pension plan. Ontario is the only jurisdiction in Canada to offer such a program. Under the OPBA,[39] the Superintendent must declare that the PBGF applies to a qualifying plan when all of the following four conditions are met:

- the plan is registered under the OPBA;

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37 By virtue of sections 84 and 85 of the OPBA and subsection 47(2) of the OBPR, there are certain benefits which are not guaranteed by the PBGF including non-funded consent benefits, non-funded special allowances, prospective benefit increases, escalated adjustment, potential early retirement window benefit values, and finally plant closure and permanent layoff benefits for which service eligibility requirements have not been met.

38 The pension benefits of the 18 pension plans (which are either municipal are unionized plans) set out in subsection 47(1) of the OPBR are not guaranteed by the PBGF.

39 See subsection 83(2) of the OPBA.

- the plan provides defined benefits that are not exempt by the OPBA or the OPBR;
- the plan is wound up in whole or in part; and
- the Superintendent is of the opinion, upon reasonable and probable grounds, that the funding requirements of the OPBA and the OPBR cannot be satisfied.

As a result, there are essentially two discretionary elements to the application of the PBGF. The first, which is really discretionary in only a very limited way, is that the plan be wound up. This need not be discretionary since an employer can cause the plan to be wound up or the Superintendent may cause the plan to be wound up,[40] provided one of several enumerated grounds for a wind up order[41] under the OPBA exist (e.g. the bankruptcy of the employer or a failure to make contributions to the pension fund). The second element of discretion, and the one that is really more meaningful, is the Superintendent must form the "opinion" that the funding requirements of the OPBA cannot be satisfied. Presumably, the Superintendent could not help but form the opinion that the funding requirements cannot be satisfied if the employer is insolvent and does not have resources to make contributions to the plan.

When the PBGF is found to apply, the Superintendent is required to allocate from the PBGF and pay to the plan sufficient amounts when combined with the assets of the plan to provide the guaranteed benefits as determined by the formula set out in the OPBR.[42] The total liability of the PBGF is limited to the assets of the PBGF,[43] however the OPBA[44] permits the Lieutenant

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40 See section 68 of the OPBA.

41 See section 69 of the OPBA.

42 See section 37 of the OPBR.

43 See section 36 of the OPBR.

44 See subsection s. 82(4) of the OPBA.

Governor in Council to authorize the Treasurer of Ontario to make loans out of the Consolidated Revenue Fund to the PBGF.

Historically, is has been a rather lengthy process to get to the stage where there is actually a payment out of the PBGF. However, on October 28, 2004, FSCO announced that it is making changes to the PBGF allocation process. Among the goals of the new process was to alleviate financial instability as a result of reductions to members' pension benefits and to expedite the transfer of funds from the PBGF to the qualifying plan. An application to the PBGF for the allocation of funds can be made once (1) the plan is declared or ordered to be wound up and (2) the Superintendent has issued a declaration that the PBGF applies to the plan. To speed up the process, the plan administration may apply for a wind up order and a PBGF declaration simultaneously. However, under the old process, a completed wind up report was required to support a declaration that the PBGF applied and for an allocation of funds from the PBGF. This requirement frequently led to delays associated with the preparation of the wind up report. Under the revised PBGF allocation process, an actuarial statement will be accepted by FSCO in lieu of a wind up report for declaration and allocation purposes under the PBGF. The revised process will also require that pension benefits to retirees be immediately reduced to the PBGF level, and not the funded level of the pension plan.

To the extent that the PBGF advances money to the pension plan to provide guaranteed benefits, the Superintendent is given a lien and charge over the assets of the employer in an equal amount[45] and the Superintendent is subrogated to the rights of the plan administrator, including the deemed trust and statutory lien claims against the employer with respect to unremitted

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45 See subsection 86(2) off the OPBA.

contributions etc.[46] However, whether the lien and charge in favour of the Superintendent will not remain enforceable in the context of CCAA or BIA proceedings is a matter of heated debate given the specific provisions of the CCAA and the BIA applicable to claims of the Crown.[47]

Despite the potential changes to the PBGF allocation process, in actual fact, the insolvency process may well be complete and the assets of the employer paid out long before any payment is made from the PBGF to the pension plan. However, it should not be discounted that one of the secondary purposes of the recent changes to the PBGF allocation process were to improve the chances of asserting a deemed trust or statutory lien claim. Given that there is still a great chance that the Superintendent will have no deemed trust or lien to assert (as contemplated by the OPBA) prior to completion of the insolvency process, it causes one to consider the question of whether the Superintendent will try to assert itself as a creditor or in some other capacity in the process of insolvency either before the plan has even been wound up or after the plan has been wound up, but before any funds have been advanced from the PBGF. The answer is "Yes". In recent materials filed in certain insolvency proceedings, the Superintendent has disclosed that very intent.

Although it remains to be seen how compelling a court will find such arguments, the basis (in simplified terms) is as follows:

- delinquent contributions or foregone contributions to a pension plan represent a "funding" of the restructuring by the plan beneficiaries and the "equities" favour granting some priority to these amounts;[48]

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46 See subsection 86(4) of the OPBA.

47 See section 86 of the BIA and section 18.4 of the CCAA which provide that all claims of Her Majesty, subject to certain exceptions, rank as unsecured claims.

- if the plan(s) have already been wound up (a rare occurrence) and are underfunded then it may be a virtual certainty that the PBGF payment in respect of the plan(s) will be made and it is only a matter of time before the statutory pre-conditions to the "PBGF" lien exist;
- the claim is "secured" and a trust claim;
- pension plan members are "involuntary creditors" and suffer a retroactive loss (since pensions accrue over time).

(d) Director and Officer Issues in Under-Funded Plans

The OPBA contains penal provisions for a breach of the OPBA by a director, officer, official or agent of a corporation and every person acting in a similar capacity.[49] Specifically, a person who "causes, authorizes, permits, acquiesces or participates in" or "fails to take all reasonable care in the circumstances" relating to a corporate offence is guilty of an offence under the PBA. Where this offence is related to the failure to make the required contributions in respect of the plan, the offender may be ordered to pay the unremitted contributions.

(e) Pre-Filing Claims

If a debtor company seeks creditor protection under the BIA or CCAA in order to effectuate a restructuring process, temporary relief, in the form of a stay of proceedings, may be available to protect directors from any liability under the OPBA. Once a notice of intention to make a proposal or a proposal is filed in BIA proceedings, creditors are stayed from commencing or

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48 This would be more compelling in circumstances where a court order is made providing funding relief of some sort during the restructuring. See the discussion of such funding relief orders below.

49 See section 110 of the OPBA.

continuing any action against a director of the debtor company that arose before the commencement of the BIA proceedings.[50] This stay of proceedings continues until the proposal, if one has been filed, is approved by the court or the corporation becomes bankrupt.[51] On the other hand, the power of the court to grant a stay of proceedings under the CCAA is discretionary.[52] A stay of proceedings granted by court order under the CCAA may also be granted to a director from any claim against the director that arose before the commencement of proceedings under the CCAA. The stay continues until a compromise or arrangement is sanctioned by the court or refused by the creditors or the court.[53]

(f) Claims Arising During the Filing

The statutory stay under the BIA and the "basic" order in CCAA will have no effect on pension funding obligations in respect of the post-filing period. Accordingly, a special order to deal both with the employer's contributions to a pension plan and the related officers and directors liability may be sought.

(g) Joint and Several Liability

Companies with plans registered in Ontario but with Quebec Members should be aware of the unique provisions in Quebec's pension legislation, the *Supplemental Pension Plans Act*[54] ("SPPA"), pertaining to multi-employer pension plans ("MEPP"). In particular the SPPA[55]

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50 See subsection 69.31(1) of the BIA.

51 See section 69 of the BIA.

52 See section 11 of the CCAA.

53 See subsection 11.5(1) of the CCAA.

54 R.S.Q. c. R-15.1.

55 See section 11 of the SPPA.

provides that a pension plan in which employees of affiliated companies participate is a MEPP unless (a) all of the corporations are affiliated and (b) the "plan provides" that all of the employers that are "parties to the plan" agree that it is not intended to be a MEPP. In such a case, the SPPA provides that each of the employers is jointly and severally liable for the obligations of the other in respect of the plan.

It is unclear how the joint and several liability requirement will be applied. In the case of a pension plan where there are multiple employers with employees in Ontario and Quebec in the pension plan, the application of the joint and several liability requirement is unclear. For instance, does it apply to obligations for only Quebec employees or does it apply to all plan members? In addition, if an employer has only Ontario members in a plan, can it nonetheless be held to be jointly liable with respect to the obligations of the Quebec employees in the event that the non-Quebec employees do not enjoy the fruits of this joint and several liability requirement?

It seems reasonable to anticipate (but far from certain) that a court would not find the Ontario employees enjoy the benefit of this provision and, therefore, the joint and several obligation should only apply to contributions with respect to the deficiency fro the Quebec employees. The last issue is really whether a non-Quebec based employer with no Quebec employees would be held to be jointly and severally liable under the provision. Common sense would suggest that if its employees do not enjoy the benefit of the contribution, then an employer should not bear the cost. It is expected that all of these issues will be litigated in the Ivaco saga commencing later this year.

(h) "Irreconcilable Differences"

One of the fundamental, underlying issues to appreciate in dealing pension plan liabilities and obligations in an insolvency restructuring effort is that the structures of the insolvency statutes and the structure of the pension standards statutes relating to funding of pension plans are based on fundamentally different notions. The pension standards legislation accommodates the fact that from time to time or at any particular point in time a pension plan will not be fully funded. However, these statutes are designed to require periodic reports taking a snapshot of the pension plan funded status and requiring a re-visitation of the levels at which future contributions will be required to meet past service promises. Indeed, it is the continual and continuous notion of pension accruals in a defined benefit plan which underlie the fundamental distinction with the insolvency statute. In a pension plan, while a contribution designed to pay for the accrual of a current service benefit is intended to satisfy that obligation, it may well turn out in the future that that obligation (now a past service obligation) may not be fully satisfied from the pension fund and so additional contributions (the special payments) are required. The insolvency statutes generally contemplate the notion of a "pre-filing claim". From an insolvency statute perspective, the entire accrued liability under the pension plan should be a pre-filing claim. However, the pension standards legislation and pension practice does not so easily unbundle the past and future elements of the pension promise – at least in respect of ongoing active employees – and calls for a continued revaluation of the assets necessary to meet that liability. Perhaps, it can be argued this has changed as a result of the *Monsanto* decision discussed earlier in the paper, since in one sense *Monsanto* stands for the proposition that on partial wind ups, individuals should be completely settled out of the pension plan. Under that construct, it isn't quite so difficult to separate various time periods or elements of the pension promise to the affected group of plan

members and to "compartmentalise them" and deal with them in the way that many other claims are dealt with. It is suggested that the way in which the competing statutes deal with pensions is either reconciled or decided in favour of the insolvency statutes on one hand or the pension and benefits standards statutes on the other hand will ultimately need to be answered and the resolution of those questions will inform the dealings with the pension issues in these circumstances.

(i) The Human Element

Of course considering these issues in a theoretical light alone fails to capture the key importance of pensions to the workforce (particularly those close to retirement) and the retirees and deferred pensioners. These people rely on the pension to sustain them and it is not surprising that they take these issues very personally. Given that a successful restructuring will be consensual and the pension stakeholders will be involved in that consensus, either through a vote or otherwise, it is fairly obvious that there will be need to engage in an effective manner with the pension stakeholders (including plan members and former members, trade unions (where applicable), pension regulators, governments of various levels who may be involved in legislating or otherwise in respect of a pension deal) to conclude any meaningful arrangement.

2. Restructuring in Insolvency

In recent years there has been much press, particularly with steel companies and airlines dealing with the topic of pension plans of insolvent companies. This portion of the paper is intended to discuss some of the issues that these circumstances present, please note it is beyond the scope of this paper to provide a detailed analysis of these very technical points.

Insolvency restructurings may have two broad outcomes – the successful restructuring, which involves the successful emergence of the corporation (or a successor corporation) from the ashes of the predecessor, or the failure of the effort leading to the effective liquidation of the corporation, either through the means of a receiver or a bankruptcy proceeding. These will be discussed in turn below.

(a) Failed Restructuring

In a failed restructuring where the corporation does not survive, it is quite likely that the wind up of the pension plan will be part of the entire process. Pension plans may be wound up by employers voluntarily at any time (subject to collective bargaining impediments) but may also be ordered to be wound up and terminated by the pension standards regulators. Generally, bankruptcy is a circumstance in which such an order may be issued by a regulator. In addition, failure to remit contributions is typically a circumstance giving rise to an ordered plan windup. Furthermore, downsizings of various levels of significance may give rise to a requirement to partially wind up a plan.

Whether it is a full or partial wind up, the liabilities related to the wind up will be required to be funded over a period that is typically five years but the period may be shorter in certain circumstances.[56] On a wind up the benefits for those persons affected by the wind up may be settled by way of lump sum transfers or the purchase of annuities. In the event that the business has failed, the continuing funding obligation of a corporation that exists in respect of an

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[56] For example, if the pension plan is subject to the OPBA and has made a qualifying plan election in accordance with section 5.1 of the OPBR, the unfunded liability may need to be eliminated by payments made over the course of a 12 month period.

underfunded plan will likely not be honoured and the employees will need to have the benefits cut back in accordance with the terms of the plan and applicable legislation.

If the contrary circumstance exists and there is a wind up and the plan is overfunded, then there may be a need to deal with the surplus (see the discussions of *Monsanto* above) and certainly will be a need to deal with it if it is a complete plan wind up. Depending upon the jurisdiction or jurisdictions in which the employees who are subject to the plan were employed, the employer (a trustee in bankruptcy) may be able to obtain a portion of the surplus if it is able to obtain the consent or agreement of the prescribed number of employees.

In the case of unfunded SERPs, an insolvency will likely prove catastrophic as the beneficiaries will qualify only as unsecured creditors and are unlikely to receive any payments. Many SERPs are secured by letters of credit and the good news is that changes to the CCAA to add section 11.2 have removed the uncertainty concerning SERPs and letters of credit arising from an early 1990's insolvency involving Woodwards' department store.[57] In that case a judge issued a temporary stay order on the calling of the letter of credit under his jurisdiction under the statute. With the statutory changes, a SERP secured through a letter of credit should be safe for the employees if properly established and administered.

Finally, if the SERP is overfunded, since it is not an RPP there is a greater likelihood that the creditors will be able to obtain a "refund" of surplus.

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[57] See 17 C.B.R. (3d) 236.

(b) Successful Restructuring

If the corporation intends to continue in business after shedding debt or otherwise compromising its liabilities, it is likely to file under the CCAA and seek to restructure its obligations in one form or another.[58] With respect to pensions and benefits matters, we have seen in the 2002 restructuring of Algoma Steel Inc. and in the more recent events involving Air Canada, Slater Steel Inc., Ivaco (query whether Slater and Ivaco qualify as successful), Stelco Inc. and United Airlines that unfunded pension obligations can be a significant burden to troubled employers and it may be necessary to reduce pension obligations or obtain some relief from the normal funding rules.

As more and more restructurings emerge with pensions as a central element, trends are developing. As a matter of very general background (from a pension lawyer speaking to the complex issues in an insolvency), the CCAA generally permits the corporation to compromise pre-filing obligations through the adoption by the necessary majority of stakeholders to the plan of arrangement presented through the process. However, post-filing obligations are not generally compromised through the CCAA process directly but may be altered through consensual arrangements with creditors and stakeholders that may be connected to the plan of arrangement (e.g. entering into a new collective agreement which meets certain cost-saving objectives may be a "condition" to a plan of arrangement). It has generally been acknowledged that compensation to employees in respect of employment in the post-filing period (i.e. current service benefits or future service benefits) can only be dealt with consensually and therefore salary and wages along with benefits are not typically changed during the restructuring period, and in any event are not

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58 The corporation would have to meet $5 million threshold under section 3 of the CCAA, or alternatively, a debtor company could file a proposal under the BIA.

typically changed without consent or at least adequate notice. With respect to pension plan contributions, it appeared that prior to 2003 the common approach was to continue funding of RPP obligations in the normal course regardless of the filing. However, more recently, aggressive approaches to pension funding during the CCAA restructuring process have been seen. Some (hopefully) representative "case studies" are discussed in further detail below to illustrate both the approach to funding during and after the filing and to review the other aspects of restrictions.

(i) Algoma I

Algoma I involved the April 1992 restructuring of Algoma Steel Ltd. into Algoma Steel Inc. This "case" also illustrates the relatively recent emergence of pension and benefit considerations as key to a successful restructuring. In this restructuring of Algoma which took place under the CCAA, the pension funding deficiency was not considered a major issue. The major issues in that restructuring were debt obligations of Algoma and environmental issues. With respect to pension and benefit obligations, the only restructuring step was to have all of the rights and obligations under the pension and benefit plans assigned from old Algoma to a new Algoma corporation that was created to facilitate the restructuring. No steps to deal with pension deficiencies were undertaken.

(ii) Algoma II

In April 2001, Algoma Steel Inc. sought and obtained protection under the CCAA for a second time. This proceeding represented by far the most comprehensive and important restructuring involving a corporation's under-funded pension plan. At the time of its filing, Algoma operated

two pension plans – one each for its hourly and salaried employees[59] and these plans operated under the so called "Section 5.1 election", being an election under the OPBR which permits employers with a plan or combined plans with assets exceeding $500 million to be excused from making special payments in respect of solvency deficiencies. At the time of the filing, the plans were not fully funded on a solvency basis and in the event that they were to be wound up, the PBGF which would have applied to virtually all of the members of the plan, would not have satisfied the full pension obligations owed to all employee and former employees.

The solution in Algoma involved the following, somewhat simplified, steps These steps are derived from the plan of arrangement that was voted on in respect of Algoma Steel Inc. that was approved and sanctioned by the court on December 19, 2001 as well as from O. Reg. 202/02 which implemented the pension plan restructuring.

1. Algoma spun off new pension plans from the original pension plans, the pension liabilities for the active workforce was assumed by these new plans and assets in respect of such liabilities were transferred from the existing plans.

2. Except as noted in Step 4 below, the obligations for the retirees and the deferred pensioners under the existing plans remained in such plans unamended, except that the provision for future inflation increases which applied to some of those individuals were no longer applicable under the plans. That is, the sole benefit compromise that occurred in the Algoma restructuring in respect of these individuals was that the possibility for future inflation related increases to their benefits was eliminated.

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[59] In Algoma's case, the majority of the salaried workforce was represented by United Steelworkers of America.

3. The existing pension plans were terminated by Algoma and a new administrator was appointed by the Superintendent. A declaration was to be made by the Superintendent that the PBGF applied to such plans. The benefits under these plans thus were capped at the level guaranteed by the PBGF.

4. With respect to the retirees and deferreds, Algoma implemented a further new pension plan which provided the shortfall in the benefits they would have had from the amended original plan (i.e. taking into account the elimination of future inflation increases) and the amount they actually received from the pension plan that is being wound up under the auspices of the Superintendent and the PBGF. This new "wrap around" pension plan had no assets to begin with and it was a requirement that the funding of such promise be satisfied over a period not exceeding 15 years.

5. Returning to the pension plans for active employees, Algoma did not enjoy a continuing Section 5.1 election in respect of such plans, these are administered by Algoma and were subject of a number of technical amendments which were intended to improve the funded position of the plans. Algoma was required to fund the deficiencies in the plan existing at the date of the pension plan restructuring over a period not exceeding 15 years. In addition, the PBGF does not apply to the new Algoma pension plans (until such time as the initial deficiency has been satisfied) and amendments thereto to improve benefits may not be made except for special early retirement window and plant closure benefits prescribed by the regulation.[60]

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60 Escalated adjustments not in excess of those under the original plans and the extension of the final average earnings formula for the previous years of employment under the Hourly Plan were also permitted.

6. In addition to the foregoing, there was the creation of a secured claim to a maximum of $100 million subordinated to (i) the "new credit facilities", the "new notes" and (iii) all charges granted from time to time by Algoma for borrowed debt or otherwise in the course of its business in favour of the continuing pension plans that may only be enforced upon Algoma's insolvency and wind up that secured the pension obligations. This security was to terminate on termination of the "new credit facilities".

The key issue in the Algoma restructuring was that the crushing funding deficiencies and pension cash flow burden on Algoma was eased because (a) a large portion of the existing pension plans were, in effect, turned over to the PBGF and it was obliged to satisfy – up to the level of "guaranteed benefits" the pre-existing shortfall in the Algoma pension plans and (b) although Algoma was required to re-commence making solvency deficiency payments to its pension plan, since the Section 5.1 election was no longer applicable, the normal 5 year period for amortization of solvency deficiency payments was stretched to 15 years. It should be appreciated that the "deal" made some commercial sense insofar as the quantum of exposure for the PBGF was mitigated by the fact that no future PBGF claims may be made under the new Algoma plans, at least until they become fully solvent.

An interesting sidebar is that the PBGF itself is funded through premiums collected from pension plans (indeed pension plans with the Section 5.1 election in place contribute several million dollars a year to the PBGF) but the accumulated amount of the PBGF at the time of Algoma II was insufficient to meet what was presumed to be all of the claims of the existing Algoma pension plans and the other claims outstanding thereon. The Lieutenant-Governor in Council is authorized, <u>but not required</u>, to advance by way of loan proceeds to the PBGF; and so in dealing with large claims or potential claims against the PBGF it is necessary to undertaken discussions

not only with the Superintendent who oversees the PBGF but also the Province of Ontario to deal with the issue of any backstopping of promises made by the PBGF or agreements made with the PBGF.

(iii) Air Canada

The story of the Air Canada restructuring saga begins with so-called "stress testing" the federal pension regulator (the "Office of the Superintendent of Financial Institutions" or OFSI) performed with respect to the Air Canada pension plans in 2003. In 2001 OFSI began stress testing federally regulated pension plans by projecting the liabilities and assets of a pension plan since the last actuarial report in order to assess the overall effect of changing market conditions on the solvency ratio of the plan. The solvency ratio is the ratio of plan assets to its solvency liabilities. If the solvency ratio was less than 1, OFSI would then consider various interventions under a unique provision of the *Pension Benefits Standards Act, 1985* ("PBSA") which OFSI has invoked to issue compliance orders where it feels the PBSA has been infringed.[61]

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[61] See section 11 of the PBSA which reads:

11. (1) If, in the opinion of the Superintendent, an administrator, an employer or any person is, in respect of a pension plan, committing or about to commit an act, or pursuing or about to pursue any course of conduct, that is contrary to safe and sound financial or business practices, the Superintendent may direct the administrator, employer or other person to

(a) cease or refrain from committing the act or pursuing the course of conduct; and

(b) perform such acts as in the opinion of the Superintendent are necessary to remedy the situation.

Directions in the case of non-compliance

(2) If, in the opinion of the Superintendent, a pension plan does not comply with this Act or the regulations or is not being administered in accordance with this Act, the regulations or the plan, the Superintendent may direct the administrator, the employer or any person to

(a) cease or refrain from committing the act or pursuing the course of conduct that constitutes the non-compliance; and

(b) perform such acts as in the opinion of the Superintendent are necessary to remedy the situation.

Opportunity for representations

In the case of Air Canada the most recent actuarial reports filed in respect of its plans (which was prepared as at January 1, 2001) indicated that the Air Canada pension plans were in a surplus position of over $915 million. As a result, and in accordance with the actuarial recommendation of that report Air Canada took contribution holidays in 2001 which continued into 2002 and 2003. In early 2003, OSFI's stress testing indicated that all of the Air Canada pension plans were in a deficit position totalling approximately $1.3 billion dollars. Based on these findings, OFSI issued a temporary direction on March 21, 2003, requiring Air Canada to remit contributions representing the normal costs of the pension funds since 2002 and directed Air Canada to cease taking contribution holidays. OSFI also took the position that the contributions that would have been made but for the contribution holidays were subject to a statutory deemed trust.[62] As a result of the temporary direction, OSFI asserted that Air Canada became liable to pay to the pension funds approximately $105 million in respect of the contribution holidays taken in 2002 and approximately $30 million in respect of contribution holidays taken in the first quarter of 2003. In a separate, but related letter dated March 21, 2003, Air Canada was also directed by OFSI to prepared new valuation reports for all Air Canada pension plans to be filed

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(3) Subject to subsection (4), no direction shall be issued under subsection (1) or (2) unless the Superintendent gives the administrator, employer or other person a reasonable opportunity to make written representations.

Temporary direction

(4) If, in the opinion of the Superintendent, the length of time required for representations to be made under subsection (3) might be prejudicial to the interests of the members, former members or any other persons entitled to pension benefits or refunds under the pension plan, the Superintendent may make a temporary direction with respect to the matters referred to in subsection (1) or (2) that has effect for a period of not more than fifteen days.

Continued effect

(5) A temporary direction under subsection (4) continues to have effect after the expiry of the fifteen day period referred to in that subsection if no representations are made to the Superintendent within that period or, if representations have been made, the Superintendent notifies the administrator, employer or other person that the Superintendent is not satisfied that there are sufficient grounds for revoking the direction.

62 See section 8 of the PBSA.

with OFSI by April 30, 2003, despite the fact that the next normal triennial actuarial report was not due until 2004. Air Canada subsequently filed for protection under the CCAA.

Ultimately, OFSI and Air Canada with the concurrence of representatives of numerous pension stakeholders agreed to a funding relief protocol and the pension plan restructuring was implemented by Regulation SOR/2004-174.[63] The key aspects to the restructuring included:

- The period to repay the solvency deficiency was increase from 5 to 10 years.
- A detailed payment schedule set out containing variable annual payments rather than equal annual payments. The earlier years of the schedule require lower payments providing Air Canada some cash flow relief.
- OFSI waived the deemed trusts it maintained were a result of the contributions required by the temporary direction but which had not been remitted by Air Canada. At the time the funding relief protocol was entered into OSFI asserted this amount was approximately $346,616,000.
- In return for OFSI's wavier of the deemed trust, Air Canada issued a secured promissory note, to the trustees of each of Air Canada's Pension Plans, with an aggregate principal amount equal to $346,616,000.
- A number of limitations were put in place including (i) restrictions on actuarial methods (no smoothing of assets to calculate the solvency assets of the plan), (ii) restrictions on the ability to increase pension or other benefits and (iii) a moratorium on contribution holidays.

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63 *Air Canada Pension Plan Solvency Deficiency Funding Regulations.*

OFSI has indicated that similar arrangements to those reached with Air Canada could be extended to other companies that enter the CCAA process. Therefore, federally regulated companies who enter the restructuring process could expect some flexibility on the part of OFSI regarding the funding of pension deficits.

(iv) Slater

On June 2, 2003, Slater Steel Inc., Slater Stainless Corp., Sorel Forge Inc., 833840 Ontario Inc., 1124207 Ontario Inc. and 3014063 Nova Scotia Company (collectively referred to as "Slater") made an application under the CCAA and an order was granted providing, among other things, a stay of proceedings against Slater. Prior to the stay being granted, Slater's pension plans were in a deficit position as indicated by the most recent actuarial valuation prepared as at December 31, 1999. Under this report, the aggregate annual contributions required to be made for all Slater pension plans was approximately $4.1 million. Slater was advised by its actuaries that the pension obligations under the next triennial actuarial valuation (as at December 31, 2002) were forecasted to increase significantly. The annual contribution (for current service costs and special payments) was expected to increase to $12.2 million annually and a one time payment of $5.9 million, which would immediately become due upon the filing of the new actuarial reports, was expected to cover the increase in normal and special payment contributions for the current year until the report is filed with FSCO (from January 1, 2003 to September 2003).

In light of these funding obligations Slater took the position, based on revised cash flow protections, that it would not have sufficient funds in the short term to satisfy the payment due immediately upon the filing of the new actuarial reports or in the long term to satisfy the ongoing pension contribution obligations. Further complicating Slater's problems was the hesitation of

the DIP lenders to provide Slater with any further financing. Slater's was also advised by its major secured creditors that they were not prepared to accept any of the risk associated with the deemed trust, statutory lien or director's charge liability which could adversely affect the priority of their security interest.

Faced with a poor cash flow situation and a lack of additional sources of funding Slater sought an extension of time from filing the new actuarial report until the expiry of the stay of proceedings under the CCAA. Formal requests to both the Ontario and Quebec pension regulators for an extension of the date for filing the new actuarial report were rejected on the basis that in each case the regulator had no authority to extend such time period. Slater then turned to the court for relief, requesting a suspension of the time period for the filing of actuarial reports until 45 days after the expiry of the stay of proceedings.

On September 15, 2003, Slater obtained an order which essentially granted its request. The comprehensive order allowed Slater to continue funding – on both a going concern and solvency basis – at the level it had been "doing" prior to the CCAA filing until 15 days after the termination date of the stay of proceedings. The issues surrounding the deemed trust, statutory lien and the directors' liability were also addressed. The relevant portions of the order are reproduced below:

> 4. THIS COURT ORDERS that,
>
> (a) any obligation upon any of the Applicants, their directors, officers, employees or any other person to file triennial actuarial valuation reports in respect of the following registered pension plans (collectively, the "pension Plans) be stayed until a date which is 15 days after the Stay Termination Date:
>
> ...
>
> (b) none of the Applicants, and their respective officers or directors shall incur any obligation, whether by way of debt, damages for breach of any duty, whether statutory, fiduciary, common law or otherwise, or for breach of trust, nor shall any trust be recognized, whether express, implied, constructive, resulting, deemed or otherwise, as a result of the failure of any person to make any contribution during the Filing Stay Period

> that they might otherwise have become required to make to any of the Pension Plans but for the stay provided herein; and
>
> (c) no lien or trust shall arise and no claim, lien or trust shall be recognized in this proceeding or in any subsequent receivership, interim receivership or bankruptcy of any of the Applicants that removes assets from the estate of the respective Applicant or that otherwise has priority over the claims of the existing Security of the Senior lending Syndicate and the DIP Charge of the DIP Lenders as set out in the Initial Order as a result of failure of any person to make any contribution during the Filing Stay Period that they might otherwise have become required to make to any of the Pension Plans but for the stay provided herein.

It is interesting to note that the court order is in the nature of a stay in respect of the obligation to file a new actuarial valuation report but appears to be a complete exemption from damages or obligations of any sort including statutory obligations with respect to failures to contribute during the filing stay period with respect to the contributions that would otherwise have been required to be made as a result of the "new" report and similarly no lien or trust will be recognised arising from such distinction and contributions. What all of this suggests is that the pre-filing claims remain and the claims which arise in respect of contributions that would have been required under the old actuarial valuation remain but that the additional amount of contributions that would have been required had the new report been filed will not give rise to a deemed trust or to other actions against the directors or Slater itself.

The assets of Slater were ultimately sold by way of asset sale in 2004, the CCAA proceedings terminated in August 2004 and a receivership order was issued. Claims against the Slater directors with respect to pension deficiencies have been advanced and rejected at the level of the Superior Court Judge presiding over the CCAA but leave to appeal to the Ontario Court of Appeal was granted on December 16, 2004.

(v) Ivaco

Not less than two weeks after the Slater order was issued, a similar motion arose from the CCAA restructuring of Ivaco Inc., Ivaco Rolling Mills Inc., Ifastgroupe Inc., IFC (Fasteners) Inc.,

Ifastgroupe Realty Inc., Docoq (1985) Corporation, Florida Sub One Holdings Inc. and 3632610 Canada Inc. (collectively referred to as "Ivaco"). The Ivaco group plans were faced with an aggregate solvency deficiency of approximately $90 million, unpaid current service contributions of approximately $2.47 million and unpaid past service contributions totalling approximately $10.1 million. After filing under the CCAA, Ivaco continued to pay current service contributions in accordance with the current actuarial report, but ceased making past service contributions. In response to correspondence from the Ontario and Quebec pension regulators concerning Ivaco's failure to remit past service contributions to the plans, Ivaco took the position that it had the discretion under the initial stay order to make its pension contributions in whole or in part and subsequently sought an order to clarify the situation.

Ivaco took the Slater order one step further by obtaining an order relieving it of the obligation to make any contributions except current service contributions. Thus all contributions relating to past service (by definition this includes all solvency contributions) are not to be made by Ivaco during the CCAA stay period. Similar to the Slater order, the order provides for protection (other than for current cost contributions) against directors liability and the deemed trust and statutory lien for the contributions that would otherwise be required during the stay period.

Developments in the Ivaco matter have continued during 2005 following the sale of the assets of the Ivaco businesses to Heico Companies LLC in 2004 resulting in the assumption by Heico of all of the union pension plans but resulting in the termination and eventual wind up of the salaried pension plans. The business creditors of the Ivaco companies had proposed to petition the companies into bankruptcy and the Superintendent of Financial Services, Ontario had sought

to resist this. In a recent judgment[64], Justice Farley rejected the Superintendent's contentions that (a) the pension plan members had "financed" the restructuring by means of the deferral or elimination of the "special payments", and (b) concluded that there was no reason to prevent the creditors from seeking to move the proceedings under the BIA even where the effect of such a step would be to defeat pension deemed trusts and statutory liens.

A number of comments in the judgment are *obiter* but suggest that at least Mr. Justice Farley is inclined to the view that pension funding deficits are pre-filing claims and to be treated as same regardless of the fact that the special payments needed to amortize deficiencies may be accorded treatment as current obligations under the OPBA. However, that status likely needs to be fully reviewed, as it may be in the pending appeal of this decision, in light of the cases relating to the interaction of federal insolvency and restructuring statutes and provincial statutes governing employment and labour relations matters.

Moreover, in other comments in the decision that are likely *obiter*, Justice Farley (a) seems to indicate that he would not exercise discretion under s. 43(7) of the BIA, as requested by the Superintendent to decline to order the petition as the typical basis for such a refusal does not emerge merely from the reversal of priorities desired by the business creditors, and (b) appears to be inclined to find that both the deemed trust and lien created by the OPBA are defeated under the BIA. However, the judge characterizes these as in the nature of comments and not final ruling. The judge also rejected characterization of the Monitor as a fiduciary in respect of the pension plans and the plan members. Finally, and not least, Justice Farley noted that since no payment have been made from the PBGF, the Superintendent had not effected or perfected its

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[64] Ivaco Inc., Re, 2005 CanLII 27605 (ON S.C.).

position as subrogee under the OPBA. This is an important comment as it responded to an argument I understand was advanced by the Superintendent that the court should accept as inevitable that there will be PBGF payment and so should consider that additional lien to exist even before an actual payment has been made from the PBGF.

(vi) United Airlines

To this point, none of restructuring case studies consider above were contested by any of the stakeholders. However, a recent pronouncement in the United Air Lines ("United") CCAA proceedings calls into question whether a court will grant relief to a debtor company from its pension obligations during a CCAA restructuring process.

United has been in Chapter 11 bankruptcy proceedings in the United States since December 11, 2002, and on May 14, 2003, United filed an application for an order under the CCAA which granted a stay of proceedings in Canada. Subsequently, on September 16, 2004, United was granted an amendment to the initial order which permitted United to cease its contributions to its pension plans. Previously United had been making the required quarterly payments until the second quarter of 2003. United's rational for ceasing its contributions was the need for additional liquidity during the restructuring process. The September order was not disputed by the CAW and OSFI, however, United's other Canadian union, the International Association of Machinists and Aerospace Workers ("IAMAW"), did not attend at the motion or consent to the order. Subsequently, in February 2005, IAMAW successful brought a motion to lift the stay of proceedings with respect to United's obligation to make contributions to its pension plans.

The principle rational for granted the IAMAW's motion was the failure of Untied to demonstrate need as had been the case in Slater and Ivaco (e.g., that it did not have sufficient funds to make

its pension funding payments or DIP arrangements were such that United could not make the required contributions to the pension plans or that it would lose directors). Based upon the 2004 actuarial report, United was required to make quarterly contributions of approximately $170,000 to its unionized DB RPP which had a solvency deficiency of approximately $202,000. The court observed that compared to the problems in the U.S.A., the size of the Canadian pension obligations were "rather insignificant" and would not have a significant impact on the U.S.A. restructuring. The court also noted that the deferral of pension funding "is not a given right of the company" and it is "achieved on a consensual basis after negotiation".

The removal of United's stay from pension contributions conceivably adds a new dimension to the way pension deficits will be addressed in future restructuring proceedings and the circumstances under which relief may be granted from the rising costs of pension benefits (such as the orders obtained by Slater and Ivaco). Arguably, an automatic stay for pension contributions will not be granted unless the debtor can establish legitimate cash flow or other concerns. However, what standards will be used to make this determination remain to be seen. The situation in United, where the pension obligations were minimal in the context, can be contrasted with the situation in Slater where the pension obligations resulted in considerable immediate and future cash obligations which would have restricted Slater's access to future funding sources and resulted in a serious impediment to the restructuring process. The consent or absence of consent or objection of the plan beneficiaries or their representatives (including trade unions), may also play an increasing role and raises further questions for consideration such as whether a stay from pension contributions will be granted where the company has demonstrated the stay is necessary for restructuring but the stay is contested by a union.

Conclusion

This has been a brief and high level review of the major issues with respect to pensions and benefits that emerge from corporate reorganisations. It is hoped that this paper will be of assistance to the reader. In the event that one is involved in a corporate reorganisation, attention to the specific facts of the event and the law prevailing at the time will need to be reviewed in detail by some one expert in the legal implications of such events. Moreover, the magnitude of today's pension deficits means that many entities seeking to restructure and to return to positive cash flow will need to address the pension issue.

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TAB 11

1995 CarswellOnt 2252, 18 C.C.P.B. 198

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1995 CarswellOnt 2252, 18 C.C.P.B. 198

Imperial Oil Ltd. v. Ontario (Superintendent of Pensions)

In the Matter of the Pension Benefits Act, R.S.O. 1990, c.P. 8 (the "Act")

In the Matter of the Decisions of the Superintendent of Pensions (the "Superintendent") dated May 7, 1993 and June 29, 1994 in respect of the Imperial Oil Limited Retirement Plan (the "IOL Plan") (1988), PN 0347054 and the Imperial Oil Limited Retirement Plan for Former Employees of McColl-Frontenac Inc. (the "MFI Plan"), PN 0344002 (collectively the "Plans")

In the Matter of a request for a Hearing before the Pension Commission of Ontario (the "Commission") in accordance with s. 89(8) of the Act regarding an amendment to s. 4.3 of the Plans

Certain members and former members of the plans represented by Koskie Minsky (the "Entitlement 55 Group") and The Superintendent of Pensions and Imperial Oil Limited

Pension Commission

Gillese, Chair; Beggs, Stephenson, Members

Heard: May 23 and 24 and July 20, 1995
Judgment: August 3, 1995
Docket: XDEC-30

Counsel: *Mr. Mark Zigler* and *Mr. Kevin MacNeil*, for the applicant.

Mr. Shaun Devlin and *Ms. Peggy McCallum*, for the Superintendent.

Mr. J. Brett Ledger and *Mr. Ian J. McSweeney*, for Imperial Oil.

Pensions --- Pensions — Administration of pension plans — Amendment of plan — General

Superintendent registered employer's amendments to employee pension plans — Amendments denied enhanced early retirement annuities to employees who had not reached age 50 at time of termination for efficiency reasons — Group of former employees brought application seeking declaration that amendments void — Application dismissed — Amendments did not violate ss. 14(1) or 22(4) of Pension Benefits Act — Termination was eligibility requirement under s. 14(1)(c) of Act — Section 22(4) of Act did not apply to act of amendment — Pension Benefits Act, R.S.O. 1990, c. P.8, ss. 14(1), 14(1)(c), 22(4).

Subsection 22(4)

26 The Entitlement 55 Group argument in relation to s. 22(4) was stated in the following terms:

> whether Imperial was faced with a conflict of interest as between its role as employer and its role as administrator; and
>
> whether Imperial acted on the conflict of interest, in its capacity as administrator of the Plans, and to the detriment of the interests of the beneficiaries of the Plans.

27 In the view of the Entitlement 55 Group, in amending s. 4.3 Imperial Oil was acting in both its capacity as employer and its capacity as administrator of the Plans, simultaneously. It recognised that Imperial Oil, as employer, had the authority to amend the pension plan as part of the employment contracts of its employees. However, it maintained that the amendment powers were subject to the fiduciary obligations imposed or created by s. 22(1) of the Act. Subsection 22(1), it was argued, imposed fiduciary obligations that were not limited to matters of fund investments but also involved plan amendments which would utilize fund assets or reduce fund liabilities "for improper purposes". The alleged improper purpose was that the Amendments reduced the potential liabilities of the pension fund in respect of individuals who would otherwise qualify.

28 At the same time, it was argued, Imperial Oil placed itself in a conflict of interest situation which is prohibited by s. 22(4); in its role as employer, it wished to reduce the pension fund liabilities but in its role as administrator it had a duty to protect the interests of the beneficiaries of the fund who had reached the 10 year service qualification and "qualified" for the s. 4.3 benefits.

29 We do not accept that Imperial Oil was acting in its capacity as administrator when it passed the Amendments and therefore we do not accept that s. 22 applied to its actions. The words "employer" and "administrator" are used throughout the Act. However, there are not used interchangeably. Rather, they are used to describe the two different functions that an employer may serve in respect of a pension plan.

30 The Act recognizes that an employer may wear "two hats" in respect of pension plans. Indeed, s. 8 specifically states that an employer may be an administrator. In that way, it acknowledges that an employer may play two roles and it is self evident that the two roles may come into conflict from time to time.

31 To illustrate how the Act uses the words "administrator" and "employer" differently throughout the Act, consider s.78 and 79 of the Act. Those provisions enable an employer to seek and receive surplus pension funds. Clearly, an administrator would be in a conflict of interest position if it sought the return of surplus funds for an employer. The Act makes it clear that it is the employer who seeks the refund of surplus funds under s. 78 and 79. In s. 19, on the other hand, it is the administrator who is charged with the obligation to ensure that "the pension plan and fund are administered in accordance with the Act and the regulations". There are many, many other instances where the Act shows that the legislature chose between the word "administrator" and "employer". This leads us to the conclusion that, at least in the first instance, when the word "administrator" is used in s. 22, it is used to mean the person or body administering the fund and who stands in a special fiduciary relationship with the plan members courtesy of the fiduciary standard of care set out in s. 22(1).

32 Is there anything in the provisions of s. 22 which would lead us to a contrary view, that is, to the view that the word "administrator" is used in s. 22 simply as a shorthand to cover all those persons and bodies that s. 8 permit to act as administrator? Not in our view. The section is aimed at setting out the standards, powers and duties, of those who wear the mantle of administrator.

33 We are of the view that an employer plays a role in respect of the pension plan that is distinct from its role as administrator. Its role as employer permits it to make the decision to create a pension plan, to amend it and to wind it up. Once the plan and fund are in place, it becomes an administrator for the purposes of management of the fund and administration of the plan. If we were to hold that an employer was an administrator for all purposes once a plan was established, of what use would a power of amendment be? An employer could never use the power to amend the plan in a way that was to its benefit, as opposed to the benefit of the employees. Section 14 presupposes this power is with an employer as it created parameters round the exercise of a power of amendment.

34 The exercise of the power of amendment was an act of Imperial Oil as employer. It breached neither s. 22(1) nor s. 22(4) as neither subsection applied to the act of amendment.

35 Another way of looking at the matter would be to see that the power of amendment contained in the Plans is an express agreement that for the purpose of making amendments, Imperial Oil would be acting in its capacity as employer.

36 Even if Imperial Oil could be seen to be the administrator when passing the Amendments, we do not accept that it infringed the rule against conflicts of interest in s. 22(4). Subsection 22(4) prohibits conflicts "in respect of the pension fund". Throughout the Act, a distinction is drawn between "administration of the plan" and "investment of the fund". Subsection 22(2), for example, refers to both administration of the plan and investment of the fund. Subsection 22(4) uses only the words "in respect of the pension fund". In so doing, it is clear that the prohibition was in respect of matters directly affecting the fund. The Amendments would admittedly have an impact on the fund. However, they were primarily about the administration of the plan and were therefore not governed by the terms of s. 22(4).

Orders

37 In light of our rulings that the amendments violated neither s. 14 nor s. 22, there is no need to consider what orders ought to be made.

Conclusion

38 The application is dismissed.

Application dismissed.

END OF DOCUMENT

TAB 12

2004 CarswellQue 2862, 2004 SCC 68, 244 D.L.R. (4th) 564, 326 N.R. 267 (Eng.), 326 N.R. 267 (Fr.), 4 C.B.R. (5th) 215, 49 B.L.R. (3d) 165, [2004] 3 S.C.R. 461, REJB 2004-72160, J.E. 2004-2016

2004 CarswellQue 2862, 2004 SCC 68, 244 D.L.R. (4th) 564, 326 N.R. 267 (Eng.), 326 N.R. 267 (Fr.), 4 C.B.R. (5th) 215, 49 B.L.R. (3d) 165, [2004] 3 S.C.R. 461, REJB 2004-72160, J.E. 2004-2016

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

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)

Supreme Court of Canada

Iacobucci,[FN*] 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 (Que. C.A.); 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 (Que. S.C.)

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)

Business associations --- Specific corporate organization matters — Directors and officers — Fiduciary duties — General principles

Even though directors implemented new inventory procurement policy that played part in corporation's bankruptcy, directors did not breach fiduciary duty under s. 122(1)(a) of Canada Business Corporations Act, which duty is not owed to creditors, in view of lack of personal interest or illegal purpose of new policy and directors' desire to make corporation better business — Duty of care under s. 122(1)(b) of Act can be owed to creditors by way of art. 1457 of

2004 CarswellQue 2862, 2004 SCC 68, 244 D.L.R. (4th) 564, 326 N.R. 267 (Eng.), 326 N.R. 267 (Fr.), 4 C.B.R. (5th) 215, 49 B.L.R. (3d) 165, [2004] 3 S.C.R. 461, REJB 2004-72160, J.E. 2004-2016

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.

2004 CarswellQue 2862, 2004 SCC 68, 244 D.L.R. (4th) 564, 326 N.R. 267 (Eng.), 326 N.R. 267 (Fr.), 4 C.B.R. (5th) 215, 49 B.L.R. (3d) 165, [2004] 3 S.C.R. 461, REJB 2004-72160, J.E. 2004-2016

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,

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> 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".

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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

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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 (Que. C.A.), *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]

TAB 13

2008 CarswellQue 12595, 2008 SCC 69, J.E. 2009-43, 71 C.P.R. (4th) 303, 52 B.L.R. (4th) 1, 383 N.R. 119, 301 D.L.R. (4th) 80, [2008] 3 S.C.R. 560

2008 CarswellQue 12595, 2008 SCC 69, J.E. 2009-43, 71 C.P.R. (4th) 303, 52 B.L.R. (4th) 1, 383 N.R. 119, 301 D.L.R. (4th) 80, [2008] 3 S.C.R. 560

BCE Inc., Re

BCE Inc. and Bell Canada (Appellants / Respondents on cross-appeals) and A Group of 1976 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Manitoba Civil Service Superannuation Board, TD Asset Management Inc. and Manulife Financial Corporation A Group of 1996 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Insurance (Canada) Limited, CIBC Global Asset Management Inc., Manitoba Civil Service Superannuation Board and TD Asset Management Inc. A Group of 1997 Debentureholders composed of: Addenda Capital Management Inc., Manulife Financial Corporation, Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Wawanesa Life Insurance Company, TD Asset Management Inc., Franklin Templeton Investments Corp. and Barclays Global Investors Canada Limited (Respondents / Appellants on cross-appeals) and Computershare Trust Company of Canada and CIBC Mellon Trust Company (Respondents) and Director Appointed Pursuant to the CBCA, Catalyst Asset Management Inc. and Matthew Stewart (Interveners)

6796508 Canada Inc. (Appellant / Respondent on cross-appeals) and A Group of 1976 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Manitoba Civil Service Superannuation Board, TD Asset Management Inc. and Manulife Financial Corporation A Group of 1996 Debentureholders composed of: Aegon Capital Management Inc., Addenda Capital Inc., Phillips, Hager & North Investment Management Ltd., Sun Life Insurance (Canada) Limited, CIBC Global Asset Management Inc., Manitoba Civil Service Superannuation Board and TD Asset Management Inc. A Group of 1997 Debentureholders composed of: Addenda Capital Management Inc., Manulife Financial Corporation, Phillips, Hager & North Investment Management Ltd., Sun Life Assurance Company of Canada, CIBC Global Asset Management Inc., Her Majesty the Queen in Right of Alberta, as represented by the Minister of Finance, Wawanesa Life Insurance Company, TD Asset Management Inc., Franklin Templeton Investments Corp. and Barclays Global Investors Canada Limited (Respondents / Appellants on cross-appeals) and Computershare Trust Company of Canada and CIBC Mellon Trust Company (Respondents) and Director Appointed Pursuant to the CBCA, Catalyst Asset Management Inc. and Matthew Stewart (Interveners)

Supreme Court of Canada

McLachlin C.J.C., Bastarache[FN*], Binnie, LeBel, Deschamps, Abella, Charron JJ.

Heard: June 17-20, 2008
Judgment: December 19, 2008
Docket: 32647

expectations.

77 It is important to note that practices and expectations can change over time. Where valid commercial reasons exist for the change and the change does not undermine the complainant's rights, there can be no reasonable expectation that directors will resist a departure from past practice: *Alberta Treasury Branches v. SevenWay Capital Corp.* (1999), 50 B.L.R. (2d) 294 (Alta. Q.B.), aff'd (2000), 8 B.L.R. (3d) 1, 2000 ABCA 194 (Alta. C.A.).

(v) Preventive Steps

78 In determining whether a stakeholder expectation is reasonable, the court may consider whether the claimant could have taken steps to protect itself against the prejudice it claims to have suffered. Thus it may be relevant to inquire whether a secured creditor claiming oppressive conduct could have negotiated protections against the prejudice suffered: *First Edmonton Place*; *SCI Systems*.

(vi) Representations and Agreements

79 Shareholder agreements may be viewed as reflecting the reasonable expectations of the parties: *Main*; *Lyall v. 147250 Canada Ltd.* (1993), 106 D.L.R. (4th) 304 (B.C. C.A.).

80 Reasonable expectations may also be affected by representations made to stakeholders or to the public in promotional material, prospectuses, offering circulars and other communications: *Tsui v. International Capital Corp.*, [1993] 4 W.W.R. 613 (Sask. Q.B.), aff'd (1993), 113 Sask. R. 3 (Sask. C.A.); *Deutsche Bank Canada v. Oxford Properties Group Inc.* (1998), 40 B.L.R. (2d) 302 (Ont. Gen. Div. [Commercial List]); *Themadel Foundation v. Third Canadian Investment Trust Ltd.* (1995), 23 O.R. (3d) 7 (Ont. Gen. Div. [Commercial List]), var'd (1998), 38 O.R. (3d) 749 (Ont. C.A.).

(vii) Fair Resolution of Conflicting Interests

81 As discussed, conflicts may arise between the interests of corporate stakeholders *inter se* and between stakeholders and the corporation. Where the conflict involves the interests of the corporation, it falls to the directors of the corporation to resolve them in accordance with their fiduciary duty to act in the best interests of the corporation, viewed as a good corporate citizen.

82 The cases on oppression, taken as a whole, confirm that the duty of the directors to act in the best interests of the corporation comprehends a duty to treat individual stakeholders affected by corporate actions equitably and fairly. There are no absolute rules. In each case, the question is whether, in all the circumstances, the directors acted in the best interests of the corporation, having regard to all relevant considerations, including, but not confined to, the need to treat affected stakeholders in a fair manner, commensurate with the corporation's duties as a responsible corporate citizen.

83 Directors may find themselves in a situation where it is impossible to please all stakeholders. 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": *Maple Leaf Foods* per Weiler J.A., at p. 192.

84 There is no principle that one set of interests — for example the interests of shareholders — should prevail over another set of interests. Everything depends on the particular situation faced by the directors and whether, having regard to that situation, they exercised business judgment in a responsible way.

85 On these appeals, it was suggested on behalf of the corporations that the "*Revlon* line" of cases from Delaware support the principle that where the interests of shareholders conflict with the interests of creditors, the interests of shareholders should prevail.

86 The "*Revlon* line" refers to a series of Delaware corporate takeover cases, the two most important of which are *Revlon Inc. v. MacAndrews & Forbes Holdings Inc.*, 506 A.2d 173 (U.S. Del. Super. 1985), and *Unocal Corp. v. Mesa Petroleum Co.*, 493 A.2d 946 (U.S. Del. S.C. 1985). In both cases, the issue was how directors should react to a hostile takeover bid. *Revlon* suggests that in such circumstances, shareholder interests should prevail over those of other stakeholders, such as creditors. *Unocal* tied this approach to situations where the corporation will not continue as a going concern, holding that although a board facing a hostile takeover "may have regard for various constituencies in discharging its responsibilities, ... such concern for non-stockholder interests is inappropriate when ... the object no longer is to protect or maintain the corporate enterprise but to sell it to the highest bidder" (p. 182).

87 What is clear is that the *Revlon* line of cases has not displaced the fundamental rule that the duty of the directors cannot be confined to particular priority rules, but is rather a function of business judgment of what is in the best interests of the corporation, in the particular situation it faces. In a review of trends in Delaware corporate jurisprudence, former Delaware Supreme Court Chief Justice E. Norman Veasey put it this way:

> [It] is important to keep in mind the precise content of this "best interests" concept — that is, to whom this duty is owed and when. Naturally, one often thinks that directors owe this duty to both the corporation and the stockholders. That formulation is harmless in most instances because of the confluence of interests, in that what is good for the corporate entity is usually derivatively good for the stockholders. There are times, of course, when the focus is directly on the interests of the stockholders [i.e., as in *Revlon*]. But, in general, the directors owe fiduciary duties to the *corporation*, not to the stockholders. [Emphasis in original.]
>
> (E. Norman Veasey with Christine T. Di Guglielmo, "What Happened in Delaware Corporate Law and Governance from 1992-2004? A Retrospective on Some Key Developments" (2005), 153 *U. Pa. L. Rev.* 1399, at p. 1431)

88 Nor does this Court's decision in *Peoples Department Stores* suggest a fixed rule that the interests of creditors must prevail. In *Peoples Department Stores*, the Court had to consider whether, in the case of a corporation under threat of bankruptcy, creditors deserved special consideration (para. 46). The Court held that the fiduciary duty to the corporation did not change in the period preceding the bankruptcy, but that if the directors breach their duty of care to a stakeholder under s. 122(1)(b) of the *CBCA*, such a stakeholder may act upon it (para. 66).

(b) Conduct which is Oppressive, is Unfairly Prejudicial or Unfairly Disregards the Claimant's Relevant Interests

89 Thus far we have discussed how a claimant establishes the first element of an action for oppression — a reasonable expectation that he or she would be treated in a certain way. However, to complete a claim for oppression, the claimant must show that the failure to meet this expectation involved unfair conduct and prejudicial consequences within s. 241 of the *CBCA*. Not every failure to meet a reasonable expectation will give rise to the equitable considerations that ground actions for oppression. The court must be satisfied that the conduct falls within the concepts of "oppression", "unfair prejudice" or "unfair disregard" of the claimant's interest, within the meaning of s. 241 of the *CBCA*. Viewed in this way, the reasonable expectations analysis that is the theoretical foundation of the oppression remedy, and the particular types of conduct described in s. 241, may be seen as complementary, rather than representing alternative approaches to the oppression remedy, as has sometimes been supposed. Together, they offer a complete picture of conduct that is unjust and inequitable, to return to the language of *Ebrahimi v. Westbourne Galleries Ltd.*.

TAB 14

Robert L. Hodgkinson *Appellant*

v.

David L. Simms and Jerry S. Waldman, carrying on business as Simms & Waldman, and the said Simms & Waldman, a partnership *Respondents*

INDEXED AS: HODGKINSON *v.* SIMMS

File No.: 23033.

1993: December 6; 1994: September 30.

Present: La Forest, L'Heureux-Dubé, Sopinka, Gonthier, McLachlin, Iacobucci and Major JJ.

ON APPEAL FROM THE COURT OF APPEAL FOR BRITISH COLUMBIA

Fiduciary duty — Non-disclosure — Damages — Financial adviser — Client insisting that adviser not be involved in promoting — Adviser not disclosing involvement in projects — Client investing in projects suggested by adviser — Ultimate decision as to whether or not to invest that of client — Substantial losses incurred during period of economic downturn — Whether or not fiduciary duty on part of adviser — If so, calculation of damages.

Contracts — Contract for independent services — Breach by failure to disclose — Calculation of damages.

Appellant, a stock broker who was inexperienced in tax planning, wanted an independent professional to advise him respecting his tax planning and tax sheltering needs. He hired respondent Simms, an accountant, who specialized in providing general tax shelter advice, and specifically, real estate tax shelter investments. Appellant relied heavily on the respondent's advice, a reliance assiduously fostered by the respondent. The relationship was such that the appellant did not really question him about the reasons underlying the advice given. Respondent advised appellant to invest in MURBs, real estate investment projects which, by the conventional wisdom, were safe and conservative. Appellant bought 4 MURBs (income tax sheltered properties) on the accountant's advice and lost heavily

Robert L. Hodgkinson *Appelant*

c.

David L. Simms et Jerry S. Waldman, exploitant une entreprise sous la raison sociale Simms & Waldman, et ladite Simms & Waldman, une société en nom collectif *Intimés*

RÉPERTORIÉ: HODGKINSON *c.* SIMMS

N° du greffe: 23033.

1993: 6 décembre; 1994: 30 septembre.

Présents: Les juges La Forest, L'Heureux-Dubé, Sopinka, Gonthier, McLachlin, Iacobucci et Major.

EN APPEL DE LA COUR D'APPEL DE LA COLOMBIE-BRITANNIQUE

Obligation fiduciaire — Non-divulgation — Dommages-intérêts — Conseiller financier — Client insistant pour que le conseiller ne fasse pas de la promotion — Non-divulgation par le conseiller de sa participation à des projets — Client investissant dans des projets recommandés par le conseiller — Décision ultime d'investir ou non revenant au client — Pertes importantes subies au cours d'une récession économique — Y avait-il obligation fiduciaire de la part du conseiller? — Dans l'affirmative, quel mode de calcul des dommages-intérêts y a-t-il lieu d'adopter?

Contrats — Contrat de services indépendants — Inexécution par omission de divulguer — Calcul des dommages-intérêts.

L'appelant, un courtier en valeurs mobilières, sans expérience dans le domaine de la planification fiscale, était à la recherche d'un professionnel indépendant qui le conseillerait relativement à ses besoins en matière de planification fiscale et d'abris fiscaux. Il a engagé l'intimé Simms, un comptable spécialisé dans la prestation de conseils généraux en matière d'abris fiscaux et, plus précisément, en matière de placements immobiliers à titre d'abris fiscaux. L'appelant se fiait énormément aux conseils de l'intimé et ce dernier encourageait assidûment cette confiance. Il n'interrogeait pas vraiment l'intimé au sujet des motifs sous-jacents des conseils fournis. L'intimé a conseillé à l'appelant d'investir dans des IRLM, des projets d'investissement immobilier qui, traditionnellement, étaient sûrs et conservateurs. Sur le

were cited by the defendants where the plaintiffs did not follow the defendants advice to buy and sell certain shares other than "Multico", the shares which in that case gave rise to the action. The court dismissed the point, stating, at p. 324: "Be that as it may, what we are here concerned with are shares of Multico." In addition, it is not without significance that in each case where the appellant invested independently of the respondent, he was in large part persuaded to invest by the personalities and track records of his co-investors. For instance, his enthusiasm for the "Akroyd II" MURB project was explained by the fact that it was his first opportunity to invest with senior management at Canarim, his new employer. While the appellant may have been a "free agent" to the extent that he wrote the cheques, the circumstances of the outside investments could easily be interpreted to support an inference of the appellant's lack of independence generally in the area of tax-related investments.

cet avis. Un point similaire a été soulevé dans l'arrêt *Elderkin*, précité, où les défendeurs avaient cité des exemples où les demandeurs n'avaient pas suivi leurs conseils relativement à l'achat et à la vente de certaines actions autres que les «Multico» qui étaient à l'origine de l'action. Le tribunal rejette ce point en affirmant, à la p. 324: [TRADUCTION] «Quoi qu'il en soit, ce qui nous intéresse en l'espèce, ce sont les actions de Multico.» En outre, il importe aussi de signaler que, chaque fois que l'appelant a investi indépendamment de l'intimé, ce sont surtout la personnalité et les antécédents de ses coinvestisseurs qui l'ont persuadé de le faire. Par exemple, il était enthousiasmé par le projet d'IRLM «Akroyd II» parce que c'était la première chance qu'il avait d'investir avec des cadres supérieurs de Canarim, son nouvel employeur. Bien que l'appelant puisse avoir été un «agent libre» dans la mesure où il tirait les chèques, on pourrait facilement interpréter les circonstances entourant les placements extérieurs de façon à inférer le manque général d'indépendance de l'appelant dans le domaine des placements de nature fiscale.

Conclusion on Fiduciary Duty Issue

To conclude, I am of the view that the trial judge did not err in finding that a fiduciary obligation existed between the parties, and that this duty was breached by the respondent's decision not to disclose pecuniary interest with the developers.

Conclusion quant à la question de l'obligation fiduciaire

En conclusion, je suis d'avis que le juge de première instance n'a pas commis d'erreur en concluant qu'il existait une obligation fiduciaire entre les parties et que l'intimé a manqué à cette obligation en ne divulguant pas son intérêt financier avec les promoteurs.

Damages

The trial judge assessed damages flowing from both breach of fiduciary duty and breach of contract. She found the quantum of damages to be the same under either claim, namely the return of capital (adjusted to take into consideration the tax benefits received as a result of the investments), plus all consequential losses, including legal and accounting fees. As I stated at the outset, I cannot find fault with the trial judge's disposition of the damages question.

Les dommages-intérêts

Le juge de première instance a évalué les dommages découlant à la fois d'un manquement à une obligation fiduciaire et d'une inexécution de contrat. Elle a conclu que le montant des dommages était le même dans les deux cas, savoir le rendement du capital (ajusté pour tenir compte des avantages fiscaux tirés des placements), plus toutes les pertes indirectes, y compris les frais de justice et de comptabilité. Comme je l'ai mentionné au début, je ne puis conclure que le juge de première instance a commis une erreur en réglant la question des dommages-intérêts.

It is useful to review some key findings of fact that bear on the issue of damages. The trial judge found the appellant paid fair market price for each of the four investments. However, she found that throughout the period during which the appellant was induced by the respondent's recommendations into making the investments, the respondent was in a financial relationship with the developers of the projects. In short, the trial judge found the respondent stood to gain financially if the appellant invested according to his recommendations. She further found that if the appellant had known of the true relationship between the respondent and the developers, he would not have invested. She also found that had the parties turned their minds to the potential consequences of the respondent's relationship with the developers it would have been reasonably foreseeable that the appellant would not have invested.

Il est utile d'examiner certaines des principales conclusions de fait qui ont une incidence sur la question des dommages-intérêts. Le juge de première instance a conclu que l'appelant a payé la juste valeur marchande pour chacun de ses quatre placements. Cependant, elle a conclu que l'intimé avait eu des rapports financiers avec les promoteurs des projets tout au long de la période où il avait, par ses recommandations, incité l'appelant à faire les placements. Bref, le juge de première instance a conclu qu'il était financièrement avantageux pour l'intimé que l'appelant investisse conformément aux recommandations qu'il lui faisait. Elle a aussi conclu que l'appelant n'aurait pas investi s'il avait été au courant des véritables rapports de l'intimé avec les promoteurs. À son avis, si les parties avaient réfléchi aux conséquences possibles des rapports de l'intimé avec les promoteurs, il aurait été raisonnablement prévisible que l'appelant n'aurait pas investi.

I turn now to the principles that bear on the calculation of damages in this case. It is well established that the proper approach to damages for breach of a fiduciary duty is restitutionary. On this approach, the appellant is entitled to be put in as good a position as he would have been in had the breach not occurred. On the facts here, this means that the appellant is entitled to be restored to the position he was in before the transaction. The trial judge adopted this restitutionary approach and fixed damages at an amount equal to the return of capital, as well as all consequential losses, minus the amount the appellant saved on income tax due to the investments.

Je passe maintenant à l'examen des principes applicables au calcul des dommages-intérêts en l'espèce. Il est bien établi qu'il convient que les dommages-intérêts, dans le cas d'un manquement à une obligation fiduciaire, soient calculés en fonction du principe de la restitution. Selon cette méthode, l'appelant a le droit d'être placé dans une position aussi bonne que celle dans laquelle il se serait trouvé en l'absence du manquement. D'après les faits en l'espèce, cela signifie que l'appelant a droit au rétablissement dans la situation où il était avant l'opération. Le juge de première instance a adopté cette méthode fondée sur la restitution et fixé les dommages-intérêts à un montant égal au rendement du capital et à toutes les pertes indirectes, moins les économies d'impôt faites par l'appelant grâce aux placements en question.

The respondent advanced two arguments against the trial judge's assessment of damages for breach of fiduciary duty. Both raise the issue of causation, and I will address these submissions as they were argued.

L'intimé a avancé deux arguments à l'encontre de l'évaluation que le juge de première instance a faite des dommages-intérêts pour manquement à une obligation fiduciaire. Les deux soulèvent la question de la causalité et je vais les examiner tels qu'ils ont été présentés.

The respondent first submitted that given the appellant's stated desire to shelter as much of his income as possible from taxation, and his practice

L'intimé a tout d'abord soutenu que l'appelant aurait quand même investi dans des abris fiscaux immobiliers s'il avait su la vérité, en raison de sa

of buying a wide variety of tax shelters, the appellant would still have invested in real-estate tax shelters had he known the true facts. The main difficulty with this submission is that it flies in the face of the facts found by the trial judge. The materiality of the non-disclosure in inducing the appellant to change his position was a live issue at trial which the judge resolved in the appellant's favour, a finding accepted by the Court of Appeal. For reasons given earlier, I agree with this finding.

What is more, the submission runs up against the long-standing equitable principle that where the plaintiff has made out a case of non-disclosure and the loss occasioned thereby is established, the onus is on the defendant to prove that the innocent victim would have suffered the same loss regardless of the breach; see *London Loan & Savings Co. v. Brickenden*, [1934] 2 W.W.R. 545 (P.C.), at pp. 550-51; see also *Huff v. Price*, *supra*, at pp. 319-20; *Commerce Capital Trust Co. v. Berk* (1989), 57 D.L.R. (4th) 759 (Ont. C.A.), at pp. 763-64. This Court recently affirmed the same principle with respect to damages at common law in the context of negligent misrepresentation; see *Rainbow Industrial Caterers Ltd. v. Canadian National Railway Co.*, [1991] 3 S.C.R. 3, at pp. 14-17. I will return to the common law cases in greater detail later; it suffices now to say that courts exercising both common law and equitable jurisdiction have approached this issue in the same manner. In *Rainbow*, Sopinka J., on behalf of a 6-1 majority of this Court, had this to say, at pp. 15-16:

> The plaintiff is the innocent victim of a misrepresentation which has induced a change of position. It is just that the plaintiff should be entitled to say "but for the tortious conduct of the defendant, I would not have changed my position". A tortfeasor who says, "Yes, but you would have assumed a position other than the *status quo ante*", and thereby asks a court to find a transaction whose terms are hypothetical and speculative, should bear the burden of displacing the plaintiff's assertion of the *status quo ante*.

volonté explicite de diminuer autant que possible son impôt et de son habitude d'acheter divers types d'abris fiscaux. La principale difficulté que pose cet argument réside dans le fait qu'il va à l'encontre des conclusions de fait du juge de première instance. La pertinence de la non-divulgation ayant amené l'appelant à changer de position était une question qui se posait en première instance et que le juge a réglée en faveur de l'appelant, laquelle conclusion a été acceptée par la Cour d'appel. Pour les motifs déjà exprimés, je suis d'accord avec cette conclusion.

Par ailleurs, cet argument va à l'encontre du principe d'*equity* établi depuis longtemps, selon lequel, si le demandeur a prouvé qu'il n'y a pas eu divulgation et qu'il en a résulté une perte, il appartient au défendeur de prouver que la victime innocente aurait subi la même perte indépendamment du manquement; voir les arrêts *London Loan & Savings Co. c. Brickenden*, [1934] 2 W.W.R. 545 (C.P.), aux pp. 550 et 551; *Huff c. Price*, précité, aux pp. 319 et 320; *Commerce Capital Trust Co. c. Berk* (1989), 57 D.L.R. (4th) 759 (C.A. Ont.), aux pp. 763 et 764. Notre Cour a récemment confirmé le même principe relativement au calcul des dommages-intérêts en common law dans le contexte d'une déclaration inexacte faite par négligence; voir l'arrêt *Rainbow Industrial Caterers Ltd. c. Compagnie des chemins de fer nationaux du Canada*, [1991] 3 R.C.S. 3, aux pp. 14 à 17. J'examinerai davantage plus loin les affaires de common law; qu'il suffise de dire pour l'instant que les tribunaux qui exercent à la fois une compétence de common law et d'*equity* ont abordé cette question de la même manière. Aux pages 15 et 16 de l'arrêt *Rainbow*, le juge Sopinka affirme ceci, au nom d'une majorité de six contre un:

> La demanderesse est la victime innocente d'une déclaration inexacte qui l'a amenée à changer sa situation. Il est juste que la demanderesse puisse alléguer que «n'eût été de la conduite délictuelle de la défenderesse, je n'aurais pas changé ma situation». L'auteur du délit civil qui répond «Oui, mais vous vous seriez mise dans une situation autre que le statu quo» et qui demande, en conséquence, au tribunal de conclure à l'existence d'un marché dont les conditions sont hypothétiques et conjecturales doit assumer le fardeau de réfuter l'allégation de statu quo de la demanderesse.

Further, mere "speculation" on the part of the defendant will not suffice; see *ibid.*, at p. 15; *Commerce Capital*, *supra*, at p. 764. In the present case the respondent has adduced no concrete evidence to "displac[e] the plaintiff's assertion of the *status quo ante*", and this submission must, therefore, be dismissed.

The respondent also argued that even assuming the appellant would not have invested had proper disclosure been made, the non-disclosure was not the proximate cause of the appellant's loss. Rather, he continued, the appellant's loss was caused by the general economic recession that hit the British Columbia real estate market in the early 1980s. The respondent submits that it is grossly unjust to hold him accountable for losses that, he maintains, have no causal relation to the breach of fiduciary duty he perpetrated on the appellant.

I observe that a similar argument was put forward and rejected in the *Kelly Peters* case, *supra*. There the plaintiffs, like the appellant in the present case, had approached the defendant investment advisors for, *inter alia*, investment advice particular to the real estate tax shelter market; see at p. 38. The defendants, like the respondent here, used their position of influence to put the plaintiffs in those specific real estate projects in which they had a pecuniary interest, namely "Kona condominiums" located in Hawaii. The plaintiffs suffered heavy losses when the real estate market for Hawaiian MURBs crashed. As I noted earlier, the defendants were eventually found liable for breach of fiduciary duties. The defendants argued that damages should be assessed with reference to the date of sale on the grounds that neither the buyer nor the seller should be affected by later market fluctuations. This argument was rejected at trial and in the Court of Appeal. In a passage cited with approval by MacFarlane J.A., the trial judge, at p. 49, stated that a purchaser has a right to recovery of losses "up to the time he learns of the

Par ailleurs, une simple «conjecture» de la part du défendeur ne suffira pas; voir, *ibid.*, à la p. 15, et l'arrêt *Commerce Capital*, précité, à la p. 764. En l'espèce, l'intimé n'a pas présenté de preuve concrète pour «réfuter l'allégation de statu quo [du] demande[ur]» et cet argument doit donc être rejeté.

L'intimé a aussi soutenu que la non-divulgation n'était pas la cause immédiate de la perte de l'appelant, même en supposant que celui-ci n'aurait pas investi s'il y avait eu divulgation appropriée. La perte de l'appelant, a-t-il poursuivi, était plutôt attribuable à la récession économique générale qui a frappé le marché immobilier de la Colombie-Britannique au début des années 80. L'intimé fait valoir qu'il est extrêmement injuste de le tenir responsable de pertes qui, selon lui, n'ont aucun lien de causalité avec le manquement à l'obligation fiduciaire qu'il a commis envers l'appelant.

Je fais remarquer qu'un argument similaire a été soulevé et avancé dans l'arrêt *Kelly Peters*, précité. Dans cette affaire, les demandeurs, à l'instar de l'appelant en l'espèce, s'étaient adressés aux conseillers financiers défendeurs pour qu'ils les avisent leur donnent notamment des conseils particuliers au marché des abris fiscaux immobiliers; voir à la p. 38. À l'instar de l'intimé en l'espèce, les défendeurs s'étaient servis de leur position d'influence pour faire participer les demandeurs à des projets immobiliers précis dans lesquels ils avaient un intérêt financier, notamment les «condominiums Kona» situés à Hawaï. Les demandeurs ont subi des pertes importantes lors de l'effondrement du marché immobilier hawaïen des IRLM. Comme je l'ai déjà mentionné, les défendeurs ont été déclarés coupables de manquement à des obligations fiduciaires. Les défendeurs ont soutenu que les dommages-intérêts devaient être évalués en fonction de la date de la vente pour le motif que ni l'acheteur ni le vendeur ne devraient être touchés par les fluctuations ultérieures du marché. Cet argument a été rejeté par le tribunal de première instance et par la Cour d'appel. Dans un passage cité et approuvé par le juge MacFarlane, le juge de première instance affirme, à la p. 49, qu'un acheteur a droit au recouvrement des pertes [TRADUC-

fraud and whether or not the losses result from a falling market".

The similarity between *Kelly Peters* and the present case is striking. Both the defendant in *Kelly Peters* and the respondent here induced parties into investments they would not otherwise have made by deliberately concealing their own financial interest. These respective investors were thereby exposed to all the risks, i.e., including the general market risks, of these investments. On the finding of facts, these investors would not have been exposed to any of the risks associated with these investments had it not been for their respective fiduciary's desire to secure an improper personal gain. In short, in each case it was the particular fiduciary breach that initiated the chain of events leading to the investor's loss. As such it is right and just that the breaching party account for this loss in full.

Contrary to the respondent's submission, this result is not affected by the *ratio* of this Court's decision in *Canson Enterprises*, *supra*. *Canson* held that a court exercising equitable jurisdiction is not precluded from considering the principles of remoteness, causation, and intervening act where necessary to reach a just and fair result. *Canson* does not, however, signal a retreat from the principle of full restitution; rather it recognizes the fact that a breach of a fiduciary duty can take a variety of forms, and as such a variety of remedial considerations may be appropriate; see also *McInerney v. MacDonald*, *supra*, at p. 149. Writing extra-judicially, Huband J.A. of the Manitoba Court of Appeal recently remarked upon this idea, in "Remedies and Restitution for Breach of Fiduciary Duties" in *The 1993 Isaac Pitblado Lectures*, *supra*, pp. 21-32, at p. 31:

A breach of a fiduciary duty can take many forms. It might be tantamount to deceit and theft, while on the other hand it may be no more than an innocent and hon-

TION] «jusqu'au moment où il est mis au courant de la fraude, et ce, que les pertes soient ou non imputables à un effondrement du marché».

Il existe une similarité frappante entre *Kelly Peters* et la présente affaire. Le défendeur dans *Kelly Peters* et l'intimé en l'espèce ont tous les deux, en dissimulant délibérément leur propre intérêt financier, incité des parties à faire des placements qu'elles n'auraient pas faits par ailleurs. Ces investisseurs se trouvaient alors exposés à tous les risques de ces placements, y compris les aléas généraux du marché. D'après les conclusions de fait, ces investisseurs n'auraient été exposés à aucun risque lié à ces placements, n'eût été la volonté de leur fiduciaire respectif de se garantir un gain personnel abusif. Bref, dans chacun de ces cas, c'est le manquement particulier à une obligation fiduciaire qui a déclenché la série d'événements qui ont abouti à la perte de l'investisseur. Il n'est donc que juste et équitable que ce soit l'auteur d'un manquement qui assume la perte en totalité.

Contrairement à que soutient l'intimé, le raisonnement de notre Cour dans l'arrêt *Canson Enterprises*, précité, ne change rien à ce résultat. Dans cet arrêt, notre Cour a statué qu'il est loisible à un tribunal qui exerce sa compétence d'*equity* d'examiner les principes de l'éloignement du dommage, de la causalité et de l'acte intermédiaire lorsque cela est nécessaire pour arriver à un résultat juste et équitable. Cet arrêt ne constitue pas cependant une indication de l'abandon du principe de la restitution intégrale; il reconnaît plutôt qu'un manquement à une obligation fiduciaire peut revêtir plusieurs formes et que divers redressements peuvent convenir; voir aussi *McInerney c. MacDonald*, précité, à la p. 149. Le juge Huband de la Cour d'appel du Manitoba a récemment fait des remarques sur cette idée dans l'article «Remedies and Restitution for Breach of Fiduciary Duties» tiré de *The 1993 Isaac Pitblado Lectures*, *loc. cit.*, pp. 21-32, à la p. 31:

[TRADUCTION] Un manquement à une obligation fiduciaire peut revêtir de nombreuses formes. Il peut équivaloir à un dol et à un vol, ou encore il peut constituer tout

est bit of bad advice, or a failure to give a timely warning.

Canson is an example of the latter type of fiduciary breach, mentioned by Huband J.A. There, the defendant solicitor failed to warn the plaintiff, his client, that the vendors and other third parties were pocketing a secret profit from a "flip" of the subject real estate such that the property was overpriced. See also *Jacks*, *supra*. In this situation, the principle of full restitution should not entitle a plaintiff to greater compensation than he or she would otherwise be entitled to at common law, wherein the limiting principles of intervening act would come into play.

Put another way, equity is not so rigid as to be susceptible to being used as a vehicle for punishing defendants with harsh damage awards out of all proportion to their actual behaviour. On the contrary, where the common law has developed a measured and just principle in response to a particular kind of wrong, equity is flexible enough to borrow from the common law. As I noted in *Canson*, at pp. 587-88, this approach is in accordance with the fusion of law and equity that occurred near the turn of the century under the auspices of the old *Judicature Acts*; see also *M. (K.) v. M. (H.)*, *supra*, at p. 61. Thus, properly understood *Canson* stands for the proposition that courts should strive to treat similar wrongs similarly, regardless of the particular cause or causes of action that may have been pleaded. As I stated in *Canson*, at p. 581:

> ... barring different policy considerations underlying one action or the other, I see no reason why the same basic claim, whether framed in terms of a common law action or an equitable remedy, should give rise to different levels of redress.

In other words, the courts should look to the harm suffered from the breach of the given duty, and apply the appropriate remedy.

Returning to the facts of the present case, one immediately notices significant differences from

au plus un mauvais conseil innocent et honnête ou un défaut de faire promptement une mise en garde.

L'arrêt *Canson* constitue un exemple de ce dernier type de manquement à une obligation fiduciaire, mentionné par le juge Huband. Dans cette affaire, l'avocat défendeur avait omis de prévenir le demandeur, son client, que les vendeurs et d'autres tierces parties tiraient un bénéfice secret d'une opération d'achat et de revente du bien immeuble en question de sorte que ce bien était trop cher. Voir aussi l'arrêt *Jacks*, précité. Dans une telle situation, le principe de la restitution intégrale ne devrait pas permettre à un demandeur d'obtenir une indemnité plus grande que celle à laquelle il aurait droit en common law où les principes restrictifs de l'acte intermédiaire entreraient en jeu.

En d'autres termes, l'*equity* n'est pas rigide au point de pouvoir être utilisée pour imposer à des défendeurs de lourds dommages-intérêts disproportionnés à leur conduite véritable. Au contraire, dans les cas où la common law a conçu un principe modéré et juste pour répondre à un type particulier de tort, l'*equity* est suffisamment souple pour emprunter à la common law. Comme je le fait remarquer aux pp. 587 et 588 dans l'arrêt *Canson*, ce point de vue est compatible avec la fusion de la common law et de l'*equity* qui a eu lieu au tournant du siècle en vertu des anciennes *Judicature Acts*; voir aussi l'arrêt *M. (K.) c. M. (H.)*, précité, à la p. 61. En conséquence, l'arrêt *Canson* signifie que les tribunaux devraient s'efforcer de traiter de façon similaire les torts similaires, quelle que soit la cause d'action invoquée. Comme je l'affirme dans l'arrêt *Canson*, à la p. 581:

> ... en l'absence de considérations de principe différentes qui sous-tendent l'une ou l'autre action, je ne vois aucune raison pour laquelle essentiellement la même demande, qu'il s'agisse d'une action en common law ou en *equity*, devrait donner lieu à différents niveaux de redressement.

En d'autres termes, les tribunaux devraient examiner le préjudice résultant du manquement à une obligation donnée et accorder le redressement approprié.

Pour revenir aux faits de la présente affaire, on se rend compte immédiatement des différences

the wrong committed by the defendant in *Canson* as compared to the character of the fiduciary breach perpetrated by the respondent. In *Canson* there was no particular nexus between the wrong complained of and the fiduciary relationship; this was underlined, at p. 577, by my colleague, McLachlin J., who followed a purely equitable route. Rather, the fiduciary relationship there arose by operation of law, and was in many ways incidental to the particular wrong. Further, the loss was caused by the wrongful act of a third party that was unrelated to the fiduciary breach. In the present case the duty the respondent breached was directly related to the risk that materialized and in fact caused the appellant's loss. The respondent had been retained specifically to seek out and make independent recommendations of suitable investments for the appellant. This agreement gave the respondent a kind of influence or discretion over the appellant in that, as the trial judge found, he effectively chose the risks to which the appellant would be exposed based on investments which in his expert opinion coincided with the appellant's overall investment objectives. In *Canson* the defendant solicitor did not advise on, choose, or exercise any control over the plaintiff's decision to invest in the impugned real estate; in short, he did not exercise any control over the risks that eventually materialized into a loss for the plaintiff.

importantes qui existent entre le tort commis par le défendeur dans l'arrêt *Canson* et le manquement à l'obligation fiduciaire commis par l'intimé en l'espèce. Dans l'arrêt *Canson*, il n'existait pas de lien particulier entre le tort dont on se plaignait et la relation fiduciaire; c'est ce que souligne, à la p. 577, ma collègue le juge McLachlin qui a adopté une démarche fondée exclusivement sur l'*equity*. Dans cette affaire, la relation fiduciaire découlait plutôt de l'effet de la loi et avait, à maints égards, un rapport secondaire avec l'acte préjudiciable particulier. Par ailleurs, la perte subie résultait de l'acte préjudiciable d'une tierce partie qui n'avait rien à voir avec le manquement à l'obligation fiduciaire. En l'espèce, l'obligation à laquelle a manqué l'intimé était directement liée au risque qui s'est réalisé et auquel est imputable la perte de l'appelant. Ce dernier avait explicitement retenu les services de l'intimé pour qu'il lui fasse des recommandations indépendantes de placements appropriés. Cette entente conférait à l'intimé une sorte d'influence ou de pouvoir discrétionnaire sur l'appelant puisque, comme l'a conclu le juge de première instance, il se trouvait effectivement à choisir les risques auxquels l'appelant serait exposé en faisant des placements qui, d'après l'opinion professionnelle de l'intimé, s'harmonisaient avec ses objectifs globaux en matière de placements. Dans l'arrêt *Canson*, l'avocat défendeur n'avait ni conseillé, ni fait de choix, ni exercé un contrôle relativement à la décision de la demanderesse d'investir dans le marché immobilier attaqué; bref, il n'avait exercé aucun contrôle sur les risques qui se sont finalement soldés par une perte pour la demanderesse.

Indeed, courts have treated common law claims of the same nature as the wrong complained of in the present case in much the same way as claims in equity. I earlier referred to *Rainbow Industrial Caterers*. The plaintiff there had contracted to cater lunches to CN employees at a certain price per meal. The price was based on the estimated number of lunches the defendant would require over the period covered by the contract. This estimate was negligently misstated, and the plaintiff suffered a significant loss. The Court was satisfied that but for the misrepresentation, the plaintiff

En fait, les tribunaux ont traité les demandes fondées sur la common law, qui portent sur le même genre de tort que celui dont on se plaint en l'espèce, sensiblement de la même façon que celles fondées sur l'*equity*. J'ai déjà mentionné l'arrêt *Rainbow Industrial Caterers*. Dans cette affaire, la demanderesse s'était engagée par contrat à fournir aux employés du CN des repas, moyennant un certain prix par repas. Ce prix avait été calculé en fonction du nombre estimatif de repas dont la défenderesse aurait besoin au cours de la période visée par le contrat. Il y a eu une déclaration

TAB 15

1995 CarswellOnt 318, 33 C.B.R. (3d) 161, 8 C.C.P.B. 1, C.E.B. & P.G.R. 8227, 8 E.T.R. (2d) 72, 31 C.C.L.I. (2d) 77, 24 O.R. (3d) 717

1995 CarswellOnt 318, 33 C.B.R. (3d) 161, 8 C.C.P.B. 1, C.E.B. & P.G.R. 8227, 8 E.T.R. (2d) 72, 31 C.C.L.I. (2d) 77, 24 O.R. (3d) 717

Canada (Attorney General) v. Confederation Life Insurance Co.

Re CONFEDERATION LIFE INSURANCE COMPANY; AND Re Insurance Companies Act, S.C. 1991, as amended; AND Re Winding-up Act, R.S.C. 1985, c. W-11, as amended

ATTORNEY GENERAL OF CANADA v. CONFEDERATION LIFE INSURANCE COMPANY

Ontario Court of Justice (General Division)

R.A. Blair J.

Heard: March 3, 7, 8, 20, 21, 27, 28 and 31 and April 5, 6 and 13, 1995
Judgment: July 4, 1995
Docket: Doc. RE 4315/94

Counsel: *Benjamin Zarnett, Andrea W. Rowe* and *Michele Altaras*, for Peat Marwick Thorne Inc., agent of Superintendent of Financial Institutions, provisional liquidator of Confederation Life Insurance Company.

Mark Zigler, Susan Rowland and *Cynthia Weekes*, appointed as representative counsel to represent interests of retirees of Confederation Life Insurance Company.

Donald C. Matheson, Q.C., Martha Milczynski and *Clifton Prophet*, appointed as representative counsel to represent interests of Supplementary Pensioners "In Pay"; and appointed as representative counsel to represent interests of Messrs. Rhind and Burns in respect of their claims for payment from Confederation Life Insurance Companies Deferred Compensation Plan.

Ronald Robertson, Q.C., Michael MacNaughton and *Edmond Lamek*, appointed as representative counsel to represent interests of Supplementary Pensioners "Not In Pay".

J.H. Grout and *Aida Van Wees*, appointed as representative counsel to represent interests of all policyholders and claimants of Confederation Life Insurance Company other than those persons described above.

Charles Scott and *David Roney*, for Canadian Life and Health Insurance Compensation Corporation.

Shaun Devlin and *Peggy McCallum*, for Superintendent of Pensions.

John Varley and *M. Jasmine Sweatman*, for Deloitte & Touche which was appointed administrator of Confederation

provision of their labour and employment services — in the context of the Retirees and Supplementary Pensioners — or from the control over and use of the funds that Messrs. Rhind and Burns elected to defer from their incomes in the years in question under the terms of the Deferred Compensation Plan.

196 As I have indicated and shall explain momentarily, however, I am not satisfied that the enrichment/detriment circumstances of this case fall within that concept as contemplated in the unjust enrichment authorities.

Absence of "Juristic Reason"

197 While a number of authorities discuss the question of what factors should be taken into account in determining whether there is an absence of juristic reason for the enrichment, none that I have reviewed deal with the question of what the phrase "juristic reason" actually means. In *Rathwell*, supra, where the phrase appears to have originated, Dickson J. used the expression "such as a contract or disposition of law" in giving examples of what could amount to "an absence of any juristic reasons ... for the enrichment" (p. 455). He considered the notion further in *Sorochan*, supra, saying (at p. 46 [emphasis added]):

> The third condition that must be satisfied before a finding of unjust enrichment can be made is also easily met on the facts of this case. There was no juristic reason for the enrichment. Mary Sorochan *was under no obligation, contractual or otherwise*, to perform the work and services in the home or on the land.

198 Cory J. was of a similar view in *Peter v. Beblow*, supra, stating at p. 363 [emphasis added]:

> When a claimant is under *no obligation contractual, statutory or otherwise to provide the work and services* to the recipient, there will be an absence of juristic reasons for the enrichment.

199 That the concept of "juristic reasons" is a broad one, involving many factors, and that it is the element in the unjust enrichment exercise which involves an examination of the "unjustness" of the situation, is apparent from the following statement of Madam Justice McLachlin in *Peter v. Beblow*, supra, at p. 645:

> It is in connection with the third element — absence of juristic reason for the enrichment — that such considerations may more properly find their place. It is at this stage that the court must consider whether the enrichment and detriment, morally neutral in themselves, are "unjust".
>
> What matters should be considered in determining whether there is an absence of juristic reason for the enrichment? The test is flexible, and the factors to be considered may vary with the situation before the court. ...
>
> In every case, the fundamental concern is the legitimate expectation of the parties ...

200 The need to consider the parties' expectations and whether retention of the benefit would be "unjust" is emphasized by Dickson J. in *Becker v. Pettkus*, supra, at pp. 848-849 and again in *Sorochan*, supra, at p. 46. "The test put forward" in this respect, according to Cory J., "is an objective one": *Peter v. Beblow*, supra, at p. 635.

201 The caselaw indicates that a contractual debtor-creditor relationship will be sufficient to establish the existence of a juristic reason for an enrichment that can be accounted for on the basis of that contrac tual relationship. I note, for example, the decision of the Saskatchewan Queen's Bench in *Royal Bank v. Pioneer Trust Co. (Liquidator of)* (1988), 68 C.B.R. (N.S.) 124 and the decision of the Ontario Court of Justice (General Division) in *Pikalo v. Morewood Industries Ltd. (Trustee of)* (1991), 7 C.B.R. (3d) 209. Both of these decisions arose in an insolvency context.

202 In *Pioneer Trust*, supra, the trust company had obtained $30,000 in cash from the Royal Bank on February 7,

1995 CarswellOnt 318, 33 C.B.R. (3d) 161, 8 C.C.P.B. 1, C.E.B. & P.G.R. 8227, 8 E.T.R. (2d) 72, 31 C.C.L.I. (2d) 77, 24 O.R. (3d) 717

1985, in exchange for a cheque in the same amount in favour of the Royal Bank. Later that day the Minister of Finance directed the Superintendent of Insurance to take control of Pioneer Trust's assets. Proceedings under the *Winding-up Act* were commenced, and a liquidator was appointed. The cheque was returned to the Royal Bank. The Royal Bank submitted a claim to the liquidator. It then brought an action, claiming, among other things, that the liquidator held the sum of $30,000 in trust for it as a constructive trustee.

203 In dealing with this claim Gerein J. readily accepted that there was an enrichment and corresponding deprivation. However, because the parties were in a debtor-creditor relationship there was a juristic reason for the enrichment. According to Gerein J. at p. 133:

> It is not unjust in law to hold the plaintiff to that status with the attendant consequences. To do otherwise would have no basis in law and would cause wrongful harm to the other creditors.

204 In *Pikalo*, supra, Chadwick J. dealt with a claim for a constructive trust by a lessor in the context of a bankruptcy of the lessee. The court viewed the lessor as an unsecured creditor and described the relationship between the parties as being "purely contractual". In holding that this fact took the claim outside the realm of constructive trust, Chadwick J. said at p. 214:

> As in most bankruptcy cases, the unsecured creditor may suffer financial hardship in the appearance of an unjust enrichment or benefit to either the bankrupt estate or a secured creditor, such as the bank in this case.

205 Finally, it appears that the absence or presence of a juristic reason in connection with the enrichment need not necessarily arise out of any relationship between the party asserting the claim for unjust enrichment and the party enriched: see *Royal Bank v. Harowitz* (1994), 17 O.R. (3d) 671 (Gen. Div.); *807933 Ontario Inc. v. Allison (Trustee of)* (1995), (sub nom. *Re Allison)* 22 O.R. (3d) 102 (Gen. Div.). This is of some significance here because it is Confederation Life's other creditors, rather than Confederation Life itself, who will "benefit" if the Company's assets are not impressed with a constructive trust to secure the Group Benefits, the supplementary retirement income arrangements and the Deferred Compensation Plan.

206 Several propositions can be distilled from the foregoing authorities respecting the concept of "juristic reason", it seems to me. They may be summarized as follows:

> (i) An obligation to make the contribution which leads to the enrichment — whether that obligation arises in a debtor-creditor or other contractual context, or whether by reason of the principles of common law or of equity, or whether it arises by way of a statutory provision — may constitute a juristic reason.
>
> (ii) The reasonable expectations of the parties must be considered, in particular, whether the party providing the contribution leading to the enrichment did so with a reasonable expectation of receiving an interest in property, and the other party knew or ought to have known of this reasonable expectation. The test in this respect is an objective one.
>
> (iii) It must be evident that the retention of the benefit would be "unjust" in the circumstances of the case.
>
> (iv) Finally, the juristic reason for the enrichment need not always be tied irrevocably to the person who asserts the unjust enrichment but may arise out of a relationship between the person enriched and some other person.

207 In short, a "juristic reason" simply means some underlying justification, grounded in a legal or equitable base, for the circumstances that have arisen, notwithstanding that the benefit/detriment equilibrium has since become unbalanced.

1995 CarswellOnt 318, 33 C.B.R. (3d) 161, 8 C.C.P.B. 1, C.E.B. & P.G.R. 8227, 8 E.T.R. (2d) 72, 31 C.C.L.I. (2d) 77, 24 O.R. (3d) 717

208 There are, as I shall outline, a number of such reasons underlying the imbalance in this case.

(b) Unjust Enrichment: Gateway to Constructive Trust

209 A finding of unjust enrichment provides a gateway to the imposition of a constructive trust. It does not automatically open the gate, however. The process is two-staged. If an unjust enrichment has occurred the next step is to determine whether the imposition of a constructive trust *is an appropriate remedy in the circumstances.*

210 At the outset it is wise, I think, to heed the caution expressed in the judgment of La Forest J. in *LAC Minerals*, supra. At pp. 677-678 (S.C.R.) he states [emphasis added]:

> I do not countenance the view that a proprietary remedy can be imposed whenever it is "just" to do so, unless further guidance can be given as to what those situations may be.
>
> . . . . .
>
> Much of the difficulty disappears if it is recognized that in this context the issue of the appropriate remedy only arises once a valid restitutionary claim has been made out. The constructive trust awards a right in property, but that right can only arise once a right to relief has been established. *In the vast majority of cases a constructive trust will not be the appropriate remedy. ... [A] constructive trust should only be awarded if there is reason to grant to the plaintiff the additional rights that flow from recognition of a right of property.*

211 The focus of the enquiry, then, should be on whether there is a justifiable reason for recognizing a right of property in the claimant, or what is tantamount to a right in property — which would be the effect in the Confederation Life context of impressing the Company's general assets with a trust to secure the Claimants' claims.

212 A number of guideposts have been established by the courts to help in navigating the path between the unjust enrichment gateway and the imposition of a constructive trust. They include:

a) whether a monetary award would be sufficient in the circumstances;

b) whether there is a sufficient factual connection or link between the contribution leading to the unjust enrichment and the property or asset in question;

c) whether the claimant reasonably expected to obtain a proprietary interest in the property or asset; and,

d) whether the competing equities point toward the imposition of a constructive trust.

Monetary Award Insufficient — The Inadequacy Consideration

213 It is obvious that a monetary award would be of little assistance to the Claimants in this case, in view of the winding-up and insolvency of Confederation Life. As Bell J. noted, in *Barnabe v. Touhey* (1994), 18 O.R. (3d) 370 (Gen. Div.) at p.379 [emphasis added]:

> In my view, none of the remedies suggested, other than the declaration of a constructive trust, would be appropriate in this case. A simple money judgment would not be a satisfactory remedy here *given the bankruptcies of Touhey and Sigouin.* In *Jesionowski v. The "Wa-Yas"*, [1993] 1 F.C. 36 at p.58, 55 F.T.R. 1 at p.27, Reed J. stated that, before a constructive trust is awarded, there must be some special reason to grant the plaintiff the additional

> rights which would flow from a right to property. She listed examples of special reasons including "a need to give priority to the plaintiff in a bankruptcy situation". I agree.

214 I think it warrants noting, however, that the mere fact of insolvency and the mere "need to give priority" to a claimant in such a situation is not, by itself, sufficient to trigger the automatic application of the constructive trust mechanism. Priority is almost always a "need" for someone in an insolvency. Tempered against the inadequacy consideration is the need to be aware of the effect of a declaration of constructive trust in such a context — the beneficiary of the trust essentially becomes a secured creditor, thus taking priority over all other unpaid general creditors. Hence the imposition of a constructive trust cannot be an automatic consideration simply because a monetary award is obviously not an adequate remedy. While priority will almost always be required by the claimant in an insolvency, it must also be just and appropriate in the circumstances to make an order that will have the effect of granting it.

A Connecting Link

215 The Supreme Court of Canada has held that in order to impose a constructive trust — and thereby, in effect, to recognize the claimant as a beneficial owner of the property in question — there must be a factual connection between the unjust enrichment and the property or asset in question.

216 Dickson J. described the requirement in *Becker v. Pettkus*, supra, at p.852, in these words [emphasis added]:

> For the unjust enrichment principle to apply it is obvious that some connection must be shown between the acquisition of property and corresponding deprivation. On the facts of this case, that test was met. The *indirect contribution of money and the direct contribution of labour is clearly linked to the acquisition of property*, the beneficial ownership of which is in dispute ... *The question is really an issue of fact: was her contribution sufficiently substantial and direct* as to entitle her to a portion of the profits realized upon the sale of the Franklin Centre property and to an interest in the Hawkesbury properties, and the beekeeping business?

217 In *Sorochan*, supra, the Chief Justice elaborated upon this view. At p.50, he said [emphasis added]:

> These cases reveal the need to retain flexibility in applying the constructive trust. In my view, the constructive trust remedy should not be confined to cases involving property acquisition. *While it is important to require that some nexus exist between the claimant's deprivation and the property in question, the link need not always take the form of a contribution to the actual acquisition of the property. A contribution relating to the preservation, maintenance or improvement of property may also suffice.* What remains primary is whether or not the services rendered have a "clear proprietary relationship", to use Professor McLeod's phrase. When such a connection is present, proprietary relief may be appropriate. ... As stated in *Pettkus* ... "The equitable principle on which the remedy of constructive trust rests is broad and general; its purpose is to prevent unjust enrichment in whatever circumstances it occurs."

218 There need not be an already recognized right of property before the constructive trust may be imposed. As a remedy, it may be used *to create* a right of property in appropriate circumstances, thus obviating the need to find a pre-existing property right by means of equitable tracing rules: see *LAC Minerals*, supra, at p.676, per La Forest J.; and *Peter v. Beblow*, supra, at p.639, per Cory J.

219 Once it is established that the claimant's contribution is "sufficiently substantial and direct" to entitle him or her to a property interest, the extent of the property interest must be determined. In general, the amount of the contribution governs the extent of the constructive trust; it must be proportionate to, or reflect the extent of, the contribution of the claimant to the property: *Becker v. Pettkus*, supra, at p.277; *Peter v. Beblow*, supra, at p.651.

Reasonable Expectations

1995 CarswellOnt 318, 33 C.B.R. (3d) 161, 8 C.C.P.B. 1, C.E.B. & P.G.R. 8227, 8 E.T.R. (2d) 72, 31 C.C.L.I. (2d) 77, 24 O.R. (3d) 717

220 Another consideration in the analysis of whether a constructive trust is the appropriate remedy is whether the claimant reasonably expected to obtain an actual proprietary interest as opposed to monetary relief: see *Sorochan*, supra, at p.52; and *Peter v. Beblow*, supra, at p.637. As stated by Dickson C.J.C. in *Sorochan* at p.52-53 [emphasis added]:

> A reasonable expectation of benefit is part and parcel of the third pre-condition of unjust enrichment (the absence of a juristic reason for the enrichment). At this point, however, in assessing whether a constructive trust remedy is appropriate, *we must direct our minds to the specific question of whether the claimant reasonably expected to receive an actual interest in property and whether the respondent was or reasonably ought to have been cognizant of that expectation.*

Competing Equities

221 Equitable remedies entail the necessity of balancing interests. In the context of a constructive trust claim against the assets of an insolvent constructive trustee, it is important to be aware of the interests of the insolvent's other creditors as well as those of the constructive trust claimant. In particular, in the context of this case, it is important to be aware of the interests of the general policyholders of Confederation Life. Widows and widowers, and those who will depend upon the viability of their life insurance policies and annuities when they become widows and widowers, are no less a group in need of protection and deserving of concern than are retired employees, supplementary pensioners and deferred compensation claimants. In fact, the statutory scheme which governs an insurance company winding-up accords them a stipulated priority. This factor cannot be ignored.

222 In *Coopérants* the Quebec Court of Appeal ascribed the following rationale to the *Winding-up Act* scheme, in a passage cited earlier (para.81 [p.228 Q.A.C.; emphasis added]):

> It would appear that the preservation of the financial security attached to an insurance policy was [the] underlying principle for the federal legislator when it stipulated that the claims of policyholders would be paid in priority in the event of the liquidation of a life insurance company. *The Winding-up Act demonstrates the desire of the legislator to protect people who put their confidence in an insurance company because they are generally institutions whose financial stability is not in doubt.*

223 In this context, then, who is it who can more readily be said to have accepted the risk of the Company's insolvency in their dealings with it? Is it the policyholders who have purchased its financial services at arm's length, putting their confidence in it in that sense as an institution "whose financial stability is not in doubt"? Or is it the Retirees, Supplementary Pensioners and Deferred Compensation Claimants, who also placed their confidence in the Company but did so more in its capacity as an employer and provider of the Employee Benefits than as a provider of institutional financial services? Some authors have suggested that one way to approach the matter of whether someone should be granted a preference over other creditors in an insolvency situation through the application of the constructive trust doctrine, is to ask whether that person, or group of persons, accepted the risk of the constructive trustee becoming insolvent: see D.M. Paciocco, "The Remedial Constructive Trust: A Principled Basis for Priorities over Creditors" (1989), 68 Can. Bar Rev. 314; J.D McCamus, "The Restitutionary Remedy of Constructive Trust" (1981) Law Society of Upper Canada, Special Lectures, *New Developments in the Law of Remedies* 89.

(c) Unjust Enrichment in Relation to the Facts Here

224

(i) The Retirees

TAB 16

1995 CarswellOnt 1167, 37 C.B.R. (3d) 73, 10 E.T.R. (2d) 68, 26 O.R. (3d) 477

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1995 CarswellOnt 1167, 37 C.B.R. (3d) 73, 10 E.T.R. (2d) 68, 26 O.R. (3d) 477

Barnabe v. Touhey

JEFFREY C. BARNABE, TERRILL C. JAMESON, TIMOTHY D. RAY, WILLIAM J.S. DEVONISH and DEREK G. NICHOLSON (applicants/respondents in appeal) v. JAMES W. TOUHEY and JOHN R. SIGOUIN (respondents/respondents in appeal)

JAMES W. TOUHEY and JOHN R. SIGOUIN (plaintiffs/respondents in appeal) v. JEFFREY C. BARNABE, TERRILL C. JAMESON, TIMOTHY D. RAY, WILLIAM J.S. DEVONISH and DEREK G. NICHOLSON (defendants/respondents in appeal); CANADIAN IMPERIAL BANK OF COMMERCE (intervenor/appellant)

Ontario Court of Appeal

McKinlay, Catzman and Abella JJ.A.

Heard: November 8-9, 1995
Judgment: November 14, 1995
Docket: Doc. CA C18932

Counsel: *Sean E. Cumming* and *Percy Ostroff*, for appellant, Canadian Imperial Bank of Commerce.

James M. O'Grady, Q.C., and *Barry Kwasniewski*, for respondent Jeffrey Barnabe.

John A. Hollander, for respondent John R. Sigouin.

Subject: Restitution; Estates and Trusts; Corporate and Commercial; Insolvency

Restitution --- Benefits arising through wrongful acts — Money or goods inequitably retained.

Trusts and Trustees --- Constructive trust.

Trusts and Trustees --- Constructive trust — Gains by fiduciaries.

Property of bankrupt — Trust property — Constructive trust — Constructive trust may have effect of granting payment to beneficiary out of fund that would otherwise be part of bankrupt's estate — Imposition of trust cannot have that result as its purpose.

The remedy of constructive trust will be imposed where there is some unjust enrichment. Such a trust must be imposed over specific property in which the person claiming the trust has reasonable expectation of obtaining an interest. While

a constructive trust, properly imposed, could have the *effect* of granting to the beneficiary of the trust payment out of funds that would otherwise become part of the bankrupt's estate divisible among his or her creditors, a constructive trust cannot be imposed for that *purpose* . To impose a trust for that purpose would amount to creating what may be a fair result between the constructive trustee and the beneficiary to the detriment of all other creditors of the bankrupt.

Appeal from judgment reported at (1994), 4 E.T.R. (2d) 22, 18 O.R. (3d) 370 (Gen. Div.) granting declaration of constructive trust.

***Per curiam*:**

1 We agree with counsel for the appellant that the order of Bell J. requiring that property of the bankrupts Touhey and Sigouin be held on a constructive trust in favour of the respondents has the effect of granting to the respondents a floating charge over all of the assets of the bankrupts in priority to the other creditors of the bankrupts.

2 We are of the opinion that the remedy of constructive trust is not appropriate in the circumstances. To dispose of this appeal, it is not necessary to refer to all of the arguments dealt with by counsel, since we are of the view that the unjust enrichment on which the constructive trust remedy is based does not exist in this case. To establish the unjust enrichment, there must be some specific property which is the subject of the enrichment, that property must have been retained by the person holding it in deprivation of the party claiming the trust, and there must be no juristic reason for the retention.

3 As to the first requirement, in this case there is no specific property which is the subject of the trust. The property ordered held comprises all of the property of the bankrupts. This alone would probably be sufficient to decide the appeal. However, we will comment on the other requirements to establish an unjust enrichment.

4 As to the second requirement, that the property must be held in deprivation of the party claiming the unjust enrichment, it is clear that the parties which are said to hold the trust property, the Canadian Imperial Bank of Commerce ("the bank") or Messrs. Touhey and Sigouin, do not hold it in deprivation of the respondents. The property said to be the subject of the trust is money which, by the order of Farley J., dated May 17, 1990, should have been paid back to the accountant administering the assets of the original "1986" partnership. The motions judge found that these monies, which were not paid back as they should have been, were deposited in the bank and used to support the operations of the new "1990" partnership. There is no evidence which clearly establishes that this money was ever paid into the account of the new partnership at the bank. However, even if it was, there is no evidence that indicates that the funds remain in the hands of the bank. Indeed, the account involved has generally been in negative balance, and, since it was an operating account of the new partnership, funds were paid in and out of the account over a period in excess of four years before the motions judge made the order imposing a constructive trust. Under those circumstances, it is almost impossible to show any true connection between funds which may have been deposited in the "1990" partnership account and the assets of that partnership or of the bankrupts. To overcome this problem, the motions judge imposed a constructive trust over all of the assets of the bankrupts. This is contrary to clear law which requires that a constructive trust be imposed over specific property in which the person claiming the trust has a reasonable expectation of obtaining a property interest. While the respondents may not have succeeded in having funds returned to the accountant by Touhey and Sigouin, as required by the order of Farley J., they were not deprived of any of the assets which were made the subject of the constructive trust. They were merely unsecured creditors of Touhey and Sigouin.

As to the third requirement, that there be no juristic reason for the retention of the property, there are at least two juristic reasons why the bank should retain the funds involved (if they were in fact deposited in the "1990" partnership account). First, the bank, through the account of the "1990" partnership, financed at least some of the operations of that partnership. In order to do so, it obtained security over the receivables and other assets of the partnership, which are subject to the order of Bell J. It was in reliance on that security that the bank financed the operations of the "1990" partnership. It was entitled to retain any funds which may have been paid into the account to reimburse it for payments

out of the account, and it was entitled to its security for the purpose of securing payment. The second juristic reason for retention of the funds is that the order of Farley J., by its terms, anticipated that the funds paid over by the accountant administering the assets of the "1986" partnership would be returned only if needed and demanded. Funds were also paid over to the other partners in the "1986" partnership, and none were required by the order to hold any funds in trust; indeed, any such order would have rendered the original payment over of no practical benefit to any of the partners.

While a constructive trust, if appropriately established, could have the *effect* of the beneficiary of the trust receiving payment out of funds which would otherwise become part of the estate of a bankrupt divisible among his creditors, a constructive trust, otherwise unavailable, cannot be imposed for that *purpose* . This would amount to imposing what may be a fair result as between the constructive trustee and beneficiary, to the unfair detriment of all other creditors of the bankrupt.

The appeal is allowed with costs, and the judgment of Bell J. is set aside to be replaced by a judgment dismissing the application with costs.

Appeal allowed.

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TAB 17

2009 CarswellBC 2787, 2009 SCC 48, [2009] B.C.W.L.D. 7641, [2009] B.C.W.L.D. 7592, [2009] B.C.W.L.D. 7593, [2009] B.C.W.L.D. 7594, [2009] B.C.W.L.D. 7464, [2009] B.C.W.L.D. 7642, [2009] B.C.W.L.D. 7589, [2009] B.C.W.L.D. 7591, [2009] B.C.W.L.D. 7473, [2009] B.C.W.L.D. 7480, J.E. 2009-1938, 97 B.C.L.R. (4th) 1, [2009] 12 W.W.R. 193, 394 N.R. 209, 70 C.C.L.T. (3d) 167, 276 B.C.A.C. 272, 468 W.A.C. 272, 312 D.L.R. (4th) 220, [2009] 3 S.C.R. 247

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2009 CarswellBC 2787, 2009 SCC 48, [2009] B.C.W.L.D. 7641, [2009] B.C.W.L.D. 7592, [2009] B.C.W.L.D. 7593, [2009] B.C.W.L.D. 7594, [2009] B.C.W.L.D. 7464, [2009] B.C.W.L.D. 7642, [2009] B.C.W.L.D. 7589, [2009] B.C.W.L.D. 7591, [2009] B.C.W.L.D. 7473, [2009] B.C.W.L.D. 7480, J.E. 2009-1938, 97 B.C.L.R. (4th) 1, [2009] 12 W.W.R. 193, 394 N.R. 209, 70 C.C.L.T. (3d) 167, 276 B.C.A.C. 272, 468 W.A.C. 272, 312 D.L.R. (4th) 220, [2009] 3 S.C.R. 247

Perez v. Galambos

Michael Z. Galambos and Michael Z. Galambos Law Corporation, both carrying on business as "Galambos & Company" and the said Galambos & Company (Appellants) and Estela Perez (Respondent)

Supreme Court of Canada

McLachlin C.J.C., Binnie, LeBel, Deschamps, Fish, Abella, Charron, Rothstein, Cromwell JJ.

Heard: April 15, 2009
Judgment: October 23, 2009[FN*]
Docket: 32586

Proceedings: reversing *Perez v. Galambos* (2008), 253 B.C.A.C. 149, 425 W.A.C. 149, 2008 BCCA 91, 78 B.C.L.R. (4th) 268, 291 D.L.R. (4th) 537, 2008 CarswellBC 339, [2008] 7 W.W.R. 39, 55 C.C.L.T. (3d) 243 (B.C. C.A.); reversing *Perez v. Galambos* (2006), 2006 BCSC 899, 2006 CarswellBC 1523 (B.C. S.C.); additional reasons at *Perez v. Galambos* (2008), 59 C.C.L.T. (3d) 15, [2008] 11 W.W.R. 197, 60 C.P.C. (6th) 3, 300 D.L.R. (4th) 329, 2008 BCCA 382, 2008 CarswellBC 2032, 83 B.C.L.R. (4th) 201, [2008] I.L.R. I-4741, 259 B.C.A.C. 310, 436 W.A.C. 310 (B.C. C.A.)

Counsel: George K. Macintosh, Q.C., Tim Dickson for Appellants

Robert D. Holmes, John W. Bilawich for Respondent

Subject: Public; Torts; Civil Practice and Procedure; Estates and Trusts; Contracts

Professions and occupations --- Barristers and solicitors — Employment of lawyer — Retainer — Extent of retainer

Plaintiff was employed by defendant law firm of defendant lawyer — Plaintiff made personal loans to firm totalling $200,000 — Plaintiff made advances voluntarily and often without firm's knowledge — During her employment, firm handled new wills for plaintiff as well as two mortgage transactions — Law firm later ceased operations and lawyer filed assignment in bankruptcy — Plaintiff was unsecured creditor and obtained nothing — Plaintiff brought action for damages for negligence, breach of fiduciary duty and breach of contract — Action was dismissed — Plaintiff was successful on appeal — Court of Appeal found that lawyer breached ad hoc fiduciary duty to plaintiff — Defendants

2009 CarswellBC 2787, 2009 SCC 48, [2009] B.C.W.L.D. 7641, [2009] B.C.W.L.D. 7592, [2009] B.C.W.L.D. 7593, [2009] B.C.W.L.D. 7594, [2009] B.C.W.L.D. 7464, [2009] B.C.W.L.D. 7642, [2009] B.C.W.L.D. 7589, [2009] B.C.W.L.D. 7591, [2009] B.C.W.L.D. 7473, [2009] B.C.W.L.D. 7480, J.E. 2009-1938, 97 B.C.L.R. (4th) 1, [2009] 12 W.W.R. 193, 394 N.R. 209, 70 C.C.L.T. (3d) 167, 276 B.C.A.C. 272, 468 W.A.C. 272, 312 D.L.R. (4th) 220, [2009] 3 S.C.R. 247

58 The Court of Appeal, however, found that the judge's finding of fact that Ms. Perez was not vulnerable to Mr. Galambos was unreasonable. The court based its reversal of the trial judge on this point on the facts that Mr. Galambos had superior legal knowledge and experience, that he understood when professional advice was needed with respect to his financial affairs, that Ms. Perez looked up to and trusted him, that there was a power imbalance in their relationship and that Ms. Perez's conduct could not be explained on the basis of simple friendship (paras. 50 and 64-65).

59 Respectfully, the reasons of the Court of Appeal disclose no basis for appellate intervention. The most that may be said is that the considerations identified by the Court of Appeal could plausibly sustain more than one conclusion about Ms. Perez's vulnerability. The Court of Appeal identified no finding of fact relevant to the judge's conclusion on this point that was both clearly wrong and determinative of the result. Rather, the Court of Appeal simply drew different inferences from the evidence than the ones drawn by the trial judge. This was not a proper basis for appellate reversal of his findings. The Court of Appeal ought not to have interfered with the judge's finding that Ms. Perez was not vulnerable to Mr. Galambos.

60 The Court of Appeal also found that the judge erred by concluding that any reliance by Ms. Perez on Mr. Galambos's statements that things would turn around was unreasonable. The court reasoned that Mr. Galambos was in the best position to assess the prospects of the firm and that Ms. Perez had no means of knowing whether the flow of work from the Department of Justice would again increase. On this basis, the court found the judge's conclusion to be "plainly wrong" (para. 61) and this error was part of the justification for appellate intervention. However, there are two difficulties with the Court of Appeal's approach to this issue.

61 First, the trial judge found as a fact that Ms. Perez did not rely on these statements (para. 53) and the Court of Appeal did not directly take issue with this finding. This makes hypothetical and irrelevant the question of whether such reliance, had it occurred, would have been reasonable; any error by the judge on this hypothetical question provides no basis for interfering with his decision. Second, even if an error on this point were pertinent to the result, the reasons of the Court of Appeal disclose no clear and determinative error in the judge's holding to the effect that any reliance would have been unreasonable. Once again, the Court of Appeal in my respectful view substituted its reading of the record for the trial judge's findings. This was not its role.

62 In summary, the trial judge's findings of fact should not have been disturbed on appeal and those findings do not support the Court of Appeal's conclusion that there was a "power-dependency" relationship between Ms. Perez and Mr. Galambos.

2. Mutual Understanding or Undertaking by the Fiduciary

63 The Court of Appeal held that, in the case of a "power-dependency" relationship, a fiduciary duty may arise even in the absence of a mutual understanding that one party would act only in the interests of the other. Respectfully, I do not agree.

64 Relying on *Hodgkinson*, the trial judge held that in order to find an *ad hoc* fiduciary duty, there must be a mutual understanding between the fiduciary and the beneficiary that the fiduciary party has relinquished his or her own self-interest and agreed to act solely on behalf of the beneficiary (para. 43). The judge concluded that there was no such mutual understanding here (para. 46). The Court of Appeal, on the other hand, held that as the relationship between Mr. Galambos and Ms. Perez was one of "power-dependency", there need not be a mutual understanding that one party has relinquished his or her own self-interest and undertaken to act in the interests of the other (para. 43). According to the Court of Appeal, what is required in the case of power- dependency relationships is proof of an expectation on the part of the plaintiff, which is reasonable in all of the circumstances, that the defendant would act in his or her best interests (para. 43). It found Ms. Perez to have such a reasonable expectation (paras. 60-65).

2009 CarswellBC 2787, 2009 SCC 48, [2009] B.C.W.L.D. 7641, [2009] B.C.W.L.D. 7592, [2009] B.C.W.L.D. 7593, [2009] B.C.W.L.D. 7594, [2009] B.C.W.L.D. 7464, [2009] B.C.W.L.D. 7642, [2009] B.C.W.L.D. 7589, [2009] B.C.W.L.D. 7591, [2009] B.C.W.L.D. 7473, [2009] B.C.W.L.D. 7480, J.E. 2009-1938, 97 B.C.L.R. (4th) 1, [2009] 12 W.W.R. 193, 394 N.R. 209, 70 C.C.L.T. (3d) 167, 276 B.C.A.C. 272, 468 W.A.C. 272, 312 D.L.R. (4th) 220, [2009] 3 S.C.R. 247

65 The appellants challenge this conclusion, submitting that one party's reasonable expectation is not sufficient and that there must be a mutual understanding that the fiduciary has undertaken to act only in the interests of the other party. Ms. Perez seeks to uphold the Court of Appeal's decision, arguing that equity is inherently flexible and that a reasonable expectation is enough in a power-dependency relationship.

66 In my view, while a mutual understanding may not always be necessary (a point we need not decide here), it is fundamental to *ad hoc* fiduciary duties that there be an undertaking by the fiduciary, which may be either express or implied, that the fiduciary will act in the best interests of the other party. In other words, while it may not be necessary for the beneficiary in all cases to consent to this undertaking, it is clearly settled that the undertaking itself is fundamental to the existence of an *ad hoc* fiduciary relationship. To explain why I have reached this conclusion, I need to go back to some basic principles of fiduciary law.

a. Some Basic Principles

67 An important focus of fiduciary law is the protection of one party against abuse of power by another in certain types of relationships or in particular circumstances. However, to assert that the protection of the vulnerable is the role of fiduciary law puts the matter too broadly. The law seeks to protect the vulnerable in many contexts and through many different doctrines. As La Forest J. noted in *Hodgkinson*, at p. 406: "[W]hereas undue influence focuses on the sufficiency of consent and unconscionability looks at the reasonableness of a given transaction, *the fiduciary principle monitors the abuse of a loyalty reposed*" (emphasis added). This brief sentence makes two important points which help sharpen the focus on the role of fiduciary law.

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

69 The second is that a critical aspect of a fiduciary relationship is an undertaking of loyalty: the fiduciary undertakes to act in the interests of the other party. This was put succinctly by McLachlin J. (as she then was) in *Norberg*, at p. 273, when she said that "fiduciary relationships... are always dependent on the fiduciary's undertaking to act in the beneficiary's interests". See also *Hodgkinson*, *per* La Forest J., at pp. 404-7.

70 Underpinning all of this is the focus of fiduciary law on relationships. As Dickson J. (as he then was) put it in *Guerin v. R.*, [1984] 2 S.C.R. 335 (S.C.C.), at p. 384: "It is the nature of the relationship ... that gives rise to the fiduciary duty." The underlying purpose of fiduciary law may be seen as protecting and reinforcing "the integrity of social institutions and enterprises", recognizing that "not all relationships are characterized by a dynamic of mutual autonomy, and that the marketplace cannot always set the rules": *Hodgkinson*, at p. 422 (*per* La Forest J.). The particular relationships on which fiduciary law focusses are those in which one party is given a discretionary power to affect the legal or vital practical interests of the other: see, e.g., *Frame v. Smith*, [1987] 2 S.C.R. 99 (S.C.C.), *per* Wilson J., at pp. 136-37; *Norberg*, *per* McLachlin J., at p. 272; Weinrib, at p. 4, quoted with approval in *Guerin*, at p. 384.

71 I return to the Court of Appeal's holding that a fiduciary duty may arise in "power-dependency" relationships

2009 CarswellBC 2787, 2009 SCC 48, [2009] B.C.W.L.D. 7641, [2009] B.C.W.L.D. 7592, [2009] B.C.W.L.D. 7593, [2009] B.C.W.L.D. 7594, [2009] B.C.W.L.D. 7464, [2009] B.C.W.L.D. 7642, [2009] B.C.W.L.D. 7589, [2009] B.C.W.L.D. 7591, [2009] B.C.W.L.D. 7473, [2009] B.C.W.L.D. 7480, J.E. 2009-1938, 97 B.C.L.R. (4th) 1, [2009] 12 W.W.R. 193, 394 N.R. 209, 70 C.C.L.T. (3d) 167, 276 B.C.A.C. 272, 468 W.A.C. 272, 312 D.L.R. (4th) 220, [2009] 3 S.C.R. 247

without any express or implied undertaking by the fiduciary to act in the best interests of the other party. I respectfully disagree with this approach, for two reasons: "power-dependency" relationships are not a special category of fiduciary relationships and the law is, in my view, clear that fiduciary duties will only be imposed on those who have expressly or impliedly undertaken them.

b. Power-Dependency Relationships as a Special Category

72 As noted by the Court of Appeal, La Forest J. used the term "power-dependency" relationships in *Norberg* and in *Hodgkinson*. In the latter case he wrote, at p. 411:

> I employed this notion, developed in an article by Professor [Phyllis] Coleman, ["Sex in Power Dependency Relationships: Taking Unfair Advantage of the 'Fair' Sex" (1988), 53 *Alb. L. Rev.* 95] to capture the dynamic of abuse in *Norberg v. Wynrib*, *supra*, at p. 255. *Norberg* concerned an aging physician who extorted sexual favours from a young female patient in exchange for feeding an addiction she had previously developed to the pain-killer Fiorinal. The difficulty in *Norberg* was that the sexual contact between the doctor and patient had the appearance of consent. However, when the pernicious effects of the situational power imbalance were considered, it was clear that true consent was absent. While the concept of a "power-dependency" relationship was there applied to an instance of sexual assault, in my view the concept accurately describes any situation where one party, by statute, agreement a particular course of conduct, or by unilateral undertaking, gains a position of overriding power or influence over another party. [Emphasis added.]

73 It is clear from these comments that La Forest J. was describing certain relationships which may also be fiduciary, but was not creating a separate category of *ad hoc* fiduciary relationships. In other words, this concept borrowed from academic writing may be useful to describe certain relationships, but it has not been and should not be used as a tool for categorization. Fiduciary relationships, he explained, are "simply a species of a broader family of relationships that may be termed "power-dependency" relationships" (p. 411). The law's approach to the situation of vulnerable people "gives rise to a variety of often overlapping duties" and "the precise legal or equitable duties the law will enforce in any given relationship are tailored to the legal and practical incidents of a particular relationship" (pp. 412-13).

74 In short, not all power-dependency relationships are fiduciary in nature, and identifying a power-dependency relationship does not, on its own, materially assist in deciding whether the relationship is fiduciary or not. It follows, in my view, that there are not and should not be special rules for recognition of fiduciary duties in the case of "power-dependency" relationships. I am therefore of the view that the Court of Appeal erred in this respect.

c. Mutual Understanding and Undertaking by the Fiduciary

75 The appellants fault the Court of Appeal for holding that fiduciary duties may arise only on the basis of the reasonable expectations of one party. The appellants say that there must be a mutual understanding that the fiduciary will act only in the interests of the other party. While I agree with the appellants that the Court of Appeal erred by basing a fiduciary obligation on Ms. Perez's reasonable expectation, it is not necessary in order to resolve this appeal to go so far as to say that a mutual understanding is necessary in all cases. It is sufficient to say here that what is required in all cases is an undertaking by the fiduciary, express or implied, to act in accordance with the duty of loyalty reposed on him or her.

76 I note that in *Hodgkinson*, this Court considered competing bases for the imposition of *ad hoc* fiduciary duties, opposing to a certain extent mutual understanding and reasonable expectations of the alleged beneficiary. While the seven judges sitting on the case were not fully unanimous in this respect, they all agreed that *ad hoc* fiduciary obligations may be imposed when there is a mutual understanding to this effect, and, following the example of Dickson J.

2009 CarswellBC 2787, 2009 SCC 48, [2009] B.C.W.L.D. 7641, [2009] B.C.W.L.D. 7592, [2009] B.C.W.L.D. 7593, [2009] B.C.W.L.D. 7594, [2009] B.C.W.L.D. 7464, [2009] B.C.W.L.D. 7642, [2009] B.C.W.L.D. 7589, [2009] B.C.W.L.D. 7591, [2009] B.C.W.L.D. 7473, [2009] B.C.W.L.D. 7480, J.E. 2009-1938, 97 B.C.L.R. (4th) 1, [2009] 12 W.W.R. 193, 394 N.R. 209, 70 C.C.L.T. (3d) 167, 276 B.C.A.C. 272, 468 W.A.C. 272, 312 D.L.R. (4th) 220, [2009] 3 S.C.R. 247

in *Guerin*, at p. 384, left the door open to such an obligation arising from a unilateral undertaking by the fiduciary (see on this point Professor Lionel Smith's insightful comment on *Hodgkinson*, "Fiduciary Relationships - Arising in Commercial Contexts - Investment Advisors: *Hodgkinson v. Simms*" (1995), 74 *Can. Bar Rev.* 714). Thus, what is required in all cases of *ad hoc* fiduciary obligations is that there be an undertaking on the part of the fiduciary to exercise a discretionary power in the interests of that other party. To repeat what was said by McLachlin J. in *Norberg*, "fiduciary relationships... are always dependent on the fiduciary's undertaking to act in the beneficiary's interests" (p. 273). As Dickson J. put it in *Guerin*, fiduciary duties may arise where "by statute, agreement, or perhaps by unilateral undertaking, one party has an obligation to act for the benefit of another" (p. 384).

77 The fiduciary's undertaking may be the result of the exercise of statutory powers, the express or implied terms of an agreement or, perhaps, simply an undertaking to act in this way. In cases of *per se* fiduciary relationships, this undertaking will be found in the nature of the category of relationship in issue. The critical point is that in both *per se* and *ad hoc* fiduciary relationships, there will be some undertaking on the part of the fiduciary to act with loyalty.

78 Commentators support this view. In his seminal work, *Fiduciary Obligations* (1977), Professor P. D. Finn writes at para. 15:

> For a person to be a fiduciary he must first and foremost have bound himself in some way to protect and/or to advance the interests of another. This is perhaps the most obvious of the characteristics of the fiduciary office for Equity will only oblige a person to act in what he believes to be another's interests if he himself has assumed a position which requires him to act for or on behalf of that other in some particular matter. [Emphasis added.]

To the same effect, Professor Smith writes in his comment on *Hodgkinson*, at p. 717 (echoing Dickson J.'s comments in *Guerin*, at p. 384, and Austin W. Scott, "The Fiduciary Principle" (1949), 37 *Cal L. Rev.* 539, at p. 540):

> The fiduciary must *relinquish* self-interest; that is an act which the fiduciary does, not an act which is done to the fiduciary. This was put slightly differently by Austin Scott, who said that "a fiduciary is a person who *undertakes* to act in the interest of another person." [Emphasis in original.]

79 This does not mean, however, that an express undertaking is required. Rather, the fiduciary's undertaking may be implied in the particular circumstances of the parties' relationship. Relevant to the enquiry of whether there is such an implied undertaking are considerations such as professional norms, industry or other common practices and whether the alleged fiduciary induced the other party into relying on the fiduciary's loyalty.

80 In my respectful view, the Court of Appeal's analysis went wrong on this point. It found a fiduciary duty without finding an undertaking, express or implied, on the part of Mr. Galambos that he would act in relation to the loans only in Ms. Perez's interests. The court's reasoning is premised on the fact that there was no such undertaking; otherwise, there would have been no need to base the conclusion that a fiduciary duty existed on Ms. Perez's expectations alone.

81 It is clear from the evidence that there was no explicit undertaking that Mr. Galambos was to act in Ms. Perez's best interest in relation to the cash advances; she does not even allege as much. Moreover, it would be inconsistent with the judge's findings to conclude that any such undertaking should be implied on the facts of this case. The trial judge found that Mr. Galambos never explicitly requested a loan and that his requests that Ms. Perez "do something" to solve the cashflow problem referred to contacting the bank to extend the firm's line of credit, which had been done several times in the past (paras. 54-55). Having never requested the advances, it is difficult to see how there was any implied undertaking to act only in Ms. Perez's interests with respect to them. The judge also found that if Ms. Perez formed any expectation that Mr. Galambos was to act as her fiduciary, it was unreasonable. Rice J. found that if there was a disparity in knowledge of the firm's finances, it was Ms. Perez who was more knowledgeable (para. 52). In such

TAB 18

2009 CarswellOnt 374, 50 C.B.R. (5th) 58, [2009] G.S.T.C. 12

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2009 CarswellOnt 374, 50 C.B.R. (5th) 58, [2009] G.S.T.C. 12

Bank of Nova Scotia v. Huronia Precision Plastics Inc.

The Bank of Nova Scotia (Applicant) v. Huronia Precision Plastics Inc. (Respondent)

Ontario Superior Court of Justice [Commercial List]

Morawetz J.

Heard: November 4, 2008
Judgment: January 26, 2009
Docket: CV-08-7722-00CL

Counsel: Sam Rappos, for Applicant, Bank of Nova Scotia

A'Amer Ather, for Canada Revenue Agency

Chris Burr, for Maxium Financial Services Inc.

Subject: Estates and Trusts; Goods and Services Tax (GST); Tax — Miscellaneous; Insolvency

Tax --- Goods and Services Tax — Collection and remittance — GST held in trust

Bank brought motion for order permanently lifting order for stay of proceedings against company to allow bank to bring application for bankruptcy order against company — Canada Revenue Agency ("CRA") also brought motion in which it sought order directing receiver to pay CRA GST debt of $63,164.17, and in event that court permitted lifting of stay, order permitting CRA to take necessary steps to protect its priority position over GST held in trust — Vesting order provided that receiver would distribute holdback of $130,000 after payment to CRA of amount of GST claim to extent that it was found to attach to net proceeds in priority to interest of bank — Bank's motion granted; CRA's dismissed — Issue was whether CRA had priority with respect to amounts over bank according to s. 222 of Excise Tax Act — Bank would have ability to nullify GST deemed trust by bringing application for bankruptcy order — Desire for bank to alter priorities was legitimate reason to seek bankruptcy — Excise Tax Act, R.S.C. 1985, c. E-15, ss. 222(1), (1.1).

Tax --- General principles — Priority of tax claims in bankruptcy proceedings

Bank brought motion for order permanently lifting order for stay of proceedings against company to allow bank to bring application for bankruptcy order against company — Canada Revenue Agency ("CRA") also brought motion in which it sought order directing receiver to pay CRA GST debt of $63,164.17, and in event that court permitted lifting

11 Counsel for BNS submits that at no time prior to or after the issuance of the Vesting Order did it accede to the CRA having an interest in the Holdback in the amount of GST Claim in absolute priority to BNS.

12 In my view, absent the wording of paragraph 9 of the Vesting Order, BNS would have the ability to reverse the priority of the GST Claim by bringing an application for a bankruptcy order.

13 The Court of Appeal decision in *Ivaco Inc., Re*, [2006] O.J. No. 4152 (Ont. C.A.) stands for the proposition that it is not improper to seek a bankruptcy order for the purpose of reversing a statutory priority. In this case, it would be to reverse the priority position of CRA. Further, the timing of BNS's action has no bearing on the validity of the action being sought as there are no such time limitations imposed under s. 222(1.1).

14 It seems to me that the issue to consider is whether paragraph 9 of the Vesting Order operates so as to support the position put forth by CRA. In my view, the paragraph is clear where it provides that the Receiver "shall distribute the Holdback, or any balance thereof, after payment to the CRA of the amount of the GST Claim *to the extent that it is found to attach to the net proceeds in priority to the interest of*... [Maxium and BNS]". [emphasis added]

15 I agree with the submission of counsel to BNS that paragraph 9 reflects that any distribution of the Holdback to CRA is dependent on a determination as to whether the GST Claim attaches to the Holdback in priority to the interest of BNS.

16 In its factum, counsel to CRA, at paragraph 24 states that the Receiver's obligation to pay the deemed trust portion of the GST was made explicit and that the obligation to pay CRA was not otherwise qualified by any conditions. I disagree. The emphasized portion of paragraph 9 has to be given a common sense interpretation which, in this case, takes into account that, at the time of the issuance of the Vesting Order, there was an outstanding issue with respect to the priority of the interest of Maxium and BNS.

17 CRA also made the submission that the Receiver had certain obligations and responsibilities as set out in paragraph 9 of the Vesting Order which specifically qualifies the Receiver's rights as set out in the Appointment Order. Counsel for CRA submitted that the relevant portion of the Vesting Order specifically speaks to payment to CRA and, as of the date of the hearing of this motion, with Huronia not being bankrupt, the Receiver is under an obligation to pay CRA the amount of its deemed trust claim. I do not read paragraph 9 in such a way that it supports this submission. At the time of the granting of the Vesting Order, the issue of priority with respect to the interest of Maxium and BNS had not been determined with finality. It follows that the payment obligation to CRA had not been triggered.

18 Paragraph 9 does not, in my view, direct the Receiver to distribute the Holdback to CRA forthwith upon the CRA providing evidence to the Receiver with respect to the amounts owing by Huronia for the period prior to the issuance of the Appointment Order. If it did, the emphasized words in paragraph 9 would serve no purpose.

19 Finally, with respect to the request of BNS to lift the stay for the purpose of bringing an application for a bankruptcy order against Huronia and authorizing the Receiver to consent to such application, I am satisfied that the desire for BNS to use the *BIA* to alter priorities is a legitimate reason to seek a bankruptcy (see *Re Ivaco Inc.*) and the timing of the BNS's action has no bearing on the validity of this request.

20 Consequently, it follows that the motion of BNS is granted and an order shall issue lifting the stay of proceedings against Huronia for the purpose of permitting BNS to bring the application for bankruptcy order and authorizing the Receiver to consent to such application on behalf of Huronia.

21 In these circumstances, it also follows that no order is to be made directing the Receiver to make payment to

CRA, nor is the stay to be lifted to enable CRA to take steps to protect its position. The motion of CRA is dismissed.

22 If the parties are unable to agree on costs, brief written submissions, to a maximum of three pages, may be filed within 20 days.

Order accordingly.

END OF DOCUMENT

TAB 19

2007 CarswellAlta 702, 2007 SCC 22, J.E. 2007-1068, [2007] A.W.L.D. 2141, [2007] A.W.L.D. 2143, [2007] A.W.L.D. 2087, 49 C.C.L.I. (4th) 1, [2007] 8 W.W.R. 1, 362 N.R. 111, 75 Alta. L.R. (4th) 1, 281 D.L.R. (4th) 125, [2007] I.L.R. I-4622, 409 A.R. 207, 402 W.A.C. 207, [2007] 2 S.C.R. 3

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2007 CarswellAlta 702, 2007 SCC 22, J.E. 2007-1068, [2007] A.W.L.D. 2141, [2007] A.W.L.D. 2143, [2007] A.W.L.D. 2087, 49 C.C.L.I. (4th) 1, [2007] 8 W.W.R. 1, 362 N.R. 111, 75 Alta. L.R. (4th) 1, 281 D.L.R. (4th) 125, [2007] I.L.R. I-4622, 409 A.R. 207, 402 W.A.C. 207, [2007] 2 S.C.R. 3

Canadian Western Bank v. Alberta

Canadian Western Bank, Bank of Montreal, Canadian Imperial Bank of Commerce, HSBC Bank Canada, National Bank of Canada, Royal Bank of Canada, Bank of Nova Scotia and Toronto-Dominion Bank (Appellants) and Her Majesty The Queen in Right of Alberta (Respondent) and Attorney General of Canada, Attorney General of Ontario, Attorney General of Quebec, Attorney General of New Brunswick, Attorney General of British Columbia, Attorney General for Saskatchewan, Alberta Insurance Council, Financial Advisors Association of Canada, AIG Life Insurance Company of Canada, Canada Life Assurance Company, La Capitale Civil Service Insurer Inc., La Capitale Insurance and Financial Services Inc., CUMIS Life Insurance Company, Desjardins Financial Security Life Assurance Company, Empire Life Insurance Company, Equitable Life Insurance Company of Canada, Great-West Life Assurance Company, Industrial Alliance Insurance and Financial Services Inc., Industrial-Alliance Pacific Life Insurance Company, London Life Insurance Company, Manufacturers Life Insurance Company, Standard Life Assurance Company of Canada, Sun Life Assurance Company of Canada and Transamerica Life Canada (Interveners)

Supreme Court of Canada

McLachlin C.J.C., Bastarache, Binnie, LeBel, Fish, Abella, Charron JJ.

Heard: April 11, 2006
Judgment: May 31, 2007
Docket: 30823

Proceedings: affirming *Canadian Western Bank v. Alberta* (2005), 18 C.C.L.I. (4th) 161, 39 Alta. L.R. (4th) 1, 361 A.R. 112, 339 W.A.C. 112, 249 D.L.R. (4th) 523, 2005 ABCA 12, 2005 CarswellAlta 28, [2005] 6 W.W.R. 226 (Alta. C.A.); affirming *Canadian Western Bank v. Alberta* (2003), 2003 ABQB 795, 2003 CarswellAlta 1356, 4 C.C.L.I. (4th) 59, 21 Alta. L.R. (4th) 22, 343 A.R. 89, [2004] 5 W.W.R. 108 (Alta. Q.B.)

Counsel: Neil Finkelstein, Jeffrey Galway, Catherine Beagan Flood for Appellants

Robert Normey, Christine Enns, Nick Parker for Respondent

Peter M. Southey for Intervener, Attorney General of Canada

Robin K. Basu, Bay Ryley for Intervener, Attorney General of Ontario

Alain Gingras for Intervener, Attorney General of Quebec

2007 CarswellAlta 702, 2007 SCC 22, J.E. 2007-1068, [2007] A.W.L.D. 2141, [2007] A.W.L.D. 2143, [2007] A.W.L.D. 2087, 49 C.C.L.I. (4th) 1, [2007] 8 W.W.R. 1, 362 N.R. 111, 75 Alta. L.R. (4th) 1, 281 D.L.R. (4th) 125, [2007] I.L.R. I-4622, 409 A.R. 207, 402 W.A.C. 207, [2007] 2 S.C.R. 3

plied. Although the doctrine is in principle applicable to all federal and provincial heads of legislative authority, the case law demonstrates that its natural area of operation is in relation to those heads of legislative authority that confer on Parliament power over enumerated federal things, people, works or undertakings. In most cases, a pith and substance analysis and the application of the doctrine of paramountcy have resolved difficulties in a satisfactory manner.

68 We turn, then, to the second branch of the appellants' argument, namely that they are relieved of compliance with provincial insurance regulations by the doctrine of federal paramountcy.

F. Doctrine of Federal Paramountcy

69 According to the doctrine of federal paramountcy, when the operational effects of provincial legislation are incompatible with federal legislation, the federal legislation must prevail and the provincial legislation is rendered inoperative to the extent of the incompatibility. The doctrine applies not only to cases in which the provincial legislature has legislated pursuant to its ancillary power to trench on an area of federal jurisdiction, but also to situations in which the provincial legislature acts within its primary powers, and Parliament pursuant to its ancillary powers. This doctrine is much better suited to contemporary Canadian federalism than is the doctrine of interjurisdictional immunity, as this Court has expressly acknowledged in the "double aspect" cases (*Mangat*, at para. 52).

70 Of course, the main difficulty consists in determining the degree of incompatibility needed to trigger the application of the doctrine of federal paramountcy. The answer the courts give to this question has become one of capital importance for the development of Canadian federalism. To interpret incompatibility broadly has the effect of expanding the powers of the central government, whereas a narrower interpretation tends to give provincial governments more latitude.

71 In developing its approach, this Court, despite the problems occasionally caused by certain relevant aspects of its case law, has shown a prudent measure of restraint in proposing strict tests: *General Motors*, at p. 669. In *Multiple Access Ltd. v. McCutcheon*, [1982] 2 S.C.R. 161 (S.C.C.), the Court defined the fundamental test for determining whether there is sufficient incompatibility to trigger the application of the doctrine of federal paramountcy. Dickson J. stated:

> In principle, there would seem to be no good reasons to speak of paramountcy and preclusion except where there is actual conflict in operation as where one enactment says "yes" and the other says "no"; "the same citizens are being told to do inconsistent things"; compliance with one is defiance of the other. [p. 191]

72 Thus, according to this test, the mere existence of a duplication of norms at the federal and provincial levels does not in itself constitute a degree of incompatibility capable of triggering the application of the doctrine. Moreover, a provincial law may in principle add requirements that supplement the requirements of federal legislation (*114957 Canada Ltée (Spraytech, Société d'arrosage*). In both cases, the laws can apply concurrently, and citizens can comply with either of them without violating the other.

73 Nevertheless, there will be cases in which imposing an obligation to comply with provincial legislation would in effect frustrate the purpose of a federal law even though it did not entail a direct violation of the federal law's provisions. The Court recognized this in *Bank of Montreal v. Hall*, [1990] 1 S.C.R. 121 (S.C.C.), in noting that Parliament's "intent" must also be taken into account in the analysis of incompatibility. The Court thus acknowledged that the impossibility of complying with two enactments is not the sole sign of incompatibility. The fact that a provincial law is incompatible with the purpose of a federal law will also be sufficient to trigger the application of the doctrine of federal paramountcy. This point was recently reaffirmed in *Mangat* and in *Rothmans, Benson & Hedges Inc. v. Saskatchewan*, [2005] 1 S.C.R. 188, 2005 SCC 13 (S.C.C.).

74 That being said, care must be taken not to give too broad a scope to *Hall*, *Mangat* and *Rothmans*. The Court has never given any indication that it intended, in those cases, to reverse its previous decisions and adopt the "occupied field" test it had clearly rejected in *O'Grady* in 1960. The fact that Parliament has legislated in respect of a matter does not lead to the presumption that in so doing it intended to rule out any possible provincial action in respect of that subject. As this Court recently

2007 CarswellAlta 702, 2007 SCC 22, J.E. 2007-1068, [2007] A.W.L.D. 2141, [2007] A.W.L.D. 2143, [2007] A.W.L.D. 2087, 49 C.C.L.I. (4th) 1, [2007] 8 W.W.R. 1, 362 N.R. 111, 75 Alta. L.R. (4th) 1, 281 D.L.R. (4th) 125, [2007] I.L.R. I-4622, 409 A.R. 207, 402 W.A.C. 207, [2007] 2 S.C.R. 3

stated, "to impute to Parliament such an intention to 'occup[y] the field' in the absence of very clear statutory language to that effect would be to stray from the path of judicial restraint in questions of paramountcy that this Court has taken since at least O'Grady " (*Rothmans*, at para. 21).

75 An incompatible federal legislative intent must be established by the party relying on it, and the courts must never lose sight of the fundamental rule of constitutional interpretation that, "[w]hen a federal statute can be properly interpreted so as not to interfere with a provincial statute, such an interpretation is to be applied in preference to another applicable construction which would bring about a conflict between the two statutes" (*Attorney General of Canada v. Law Society of British Columbia*, at p. 356). To sum up, the onus is on the party relying on the doctrine of federal paramountcy to demonstrate that the federal and provincial laws are in fact incompatible by establishing either that it is impossible to comply with both laws or that to apply the provincial law would frustrate the purpose of the federal law.

G. Order of Application of the Constitutional Doctrines

76 The above review of constitutional doctrines inevitably raises questions about the logical order in which they should be applied. It would be difficult to avoid beginning with the "pith and substance" analysis, which serves to determine whether the legislation in question is in fact *valid*. The other two doctrines serve merely to determine whether a valid law is *applicable* or *operative* in specific circumstances.

77 Although our colleague Bastarache J. takes a different view on this point, we do not think it appropriate to *always* begin by considering the doctrine of interjurisdictional immunity. To do so could mire the Court in a rather abstract discussion of "cores" and "vital and essential" parts to little practical effect. As we have already noted, interjurisdictional immunity is of limited application and should in general be reserved for situations already covered by precedent. This means, in practice, that it will be largely reserved for those heads of power that deal with federal things, persons or undertakings, or where in the past its application has been considered absolutely indispensable or necessary to enable Parliament or a provincial legislature to achieve the purpose for which exclusive legislative jurisdiction was conferred, as discerned from the constitutional division of powers as a whole, or what is absolutely indispensable or necessary to enable an undertaking to carry out its mandate in what makes it specifically of federal (or provincial) jurisdiction. If a case can be resolved by the application of a pith and substance analysis, and federal paramountcy where necessary, it would be preferable to take that approach, as this Court did in *Mangat*.

78 In the result, while in theory a consideration of interjurisdictional immunity is apt for consideration after the pith and substance analysis, in practice the absence of prior case law favouring its application to the subject matter at hand will generally justify a court proceeding directly to the consideration of federal paramountcy.

H. Application to the Facts of this Case

79 While the particular factual elements of this case have already been canvassed for the purpose of the legal analysis, we will address them in greater depth out of respect for the detailed arguments of the parties.

(1) The Pith and Substance of the Alberta Insurance Act Relates to Property and Civil Rights in the Province

80 The Alberta *Insurance Act* is a valid law. As the banks acknowledge, the business of insurance in general falls within the authority of the provinces as a matter of property and civil rights. See, e.g., *Parsons* and *Canadian Pioneer Management*. As noted earlier, a federally incorporated company remains subject to provincial regulation in respect of its insurance business: *Canadian Indemnity*. The banks say however that the promotion of their eight lines of "authorized" insurance products is integral to their lending practices, and thus to banking, which is a federally regulated activity.

81 Nevertheless, banks, as such, are not exempt from provincial law. In *Bank of Toronto v. Lambe*, as mentioned earlier, it was held that the bank was subject to a provincial tax aimed at banks. In *Gregory Co. v. Imperial Bank of Canada* (1959), [1960] C.S. 204 (Que. S.C.), it was held by the Quebec Superior Court that a bank is subject to provincial securities laws.

TAB 20

2007 CarswellOnt 7014, 63 C.C.P.B. 125, 37 C.B.R. (5th) 282, 161 A.C.W.S. (3d) 675

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2007 CarswellOnt 7014, 63 C.C.P.B. 125, 37 C.B.R. (5th) 282, 161 A.C.W.S. (3d) 675

Collins & Aikman Automotive Canada Inc., Re

IN THE MATTER OF the Companies Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

AND IN THE MATTER OF a Plan of Compromise or Arrangement of COLLINS & AIKMAN AUTOMOTIVE CANADA INC.

APPLICATION UNDER the Companies Creditors Arrangement Act, R.S.C. 1985, c. C-36, as amended

Ontario Superior Court of Justice

Spence J.

Heard: September 20, 26, 2007
Judgment: October 31, 2007
Docket: 07-CL-7105

Counsel: M.E. Bailey for Superintendent of Financial Services (Ontario)

K.T. Rosenberg, M.C. Starnino for United Steelworkers

C.E. Sinclair for National Automobile, Aerospace, Transportation and General Workers Union of Canada (CAW — Canada)

R.J. Chadwick for Ernst & Young Inc., as Monitor of Collins & Aikman Automotive Canada Inc.

A.J. Taylor, K.L. Mah for Collins & Aikman Automotive Canada Inc.

J.E. Dacks for JP Morgan Chase Bank NA

C.J. Hill for Chrysler LLC

Subject: Insolvency; Corporate and Commercial; Labour and Employment; Public

Bankruptcy and insolvency --- Proposal — Companies' Creditors Arrangement Act — Miscellaneous issues

Motions to amend initial order — Insolvent company filed under Companies' Creditors Arrangement Act ("CCAA") — Company's customer became debtor in possession ("DIP") lender pursuant to funding agreement between creditors — Court

89 Accordingly, this point does not alter the conclusion that the Court has the jurisdiction to approve the "not required" clause, notwithstanding its effect in respect of the special payments.

Exercise of the Statutory Discretion under the CCAA

90 There is a separate question raised whether it is a proper exercise of the discretion of the court for it to approve the provision in question. That question must be addressed in the context discussed above.

91 The evidence before this Court is that Automotive is incapable of making the special payments. Automotive does not have the funds necessary to make the special payments. As at July 19, 2007, Automotive had no cash of its own. In the five-week period from July 19, 2007 to August 25, 2007, Automotive had negative cash flow from operations of approximately $5 million. It is forecast that in the four-week period from August 26, 2007 until September 22, 2007 Automotive will have negative cash flow of approximately an additional $12 million. Since filing, Automotive has been wholly dependent on the DIP Loan to fund all disbursements.

92 Two other important considerations are evident in the present case. First, for the reasons given above, the effective suspension of special payments is a feature of the integrated arrangement which was made available by Chrysler as the DIP Lender and which was the arrangement which enabled the company to continue in operation. So there was and is a very good reason for the Court to approve that arrangement.

93 Secondly, the moving parties each had a full opportunity to object to the approval of the DIP Facility and none of them did so, even though it was clear from the terms of the DIP Facility and the terms of the Initial Order that they are an integrated arrangement. Instead of objecting to the DIP Facility, they have allowed it to be approved and have objected only to the related provisions of the Initial Order. In proceeding this way, it appears they have avoided facing the question whether if they opposed the DIP Approval Order for the reasons they now advance in respect of the special payments, the DIP Lender might have resisted their demands at the first moment, to the detriment of the continuing employment of members, and they now seek to raise the issue now that the DIP lender is in place and has been advancing funds, in circumstances where the only practical consequence could be to raise the question which would have appropriately been raised at the earlier stage.

94 Chrysler submitted that this conduct is a collateral attack on the DIP Approval Order and should not be countenanced by the Court.

95 The Initial Order was approved on July 19, 2007 with a provision in paragraph 3 providing for a further hearing on July 30, 2007 (the "Comeback Date") at which time the Initial Order could be supplemented or otherwise varied. On July 30, 2007 the Court ordered the approval of the DIP Facility. It ordered an extension of the Stay Period to August 24, 2007.

96 The Court did not make any order to supplement or vary the Initial Order in any other respects. Neither did it make any order to the contrary. Nor does it appear from the recitals in the DIP Approval Order that the Court was asked on that motion to deal with the Initial Order in other respects. Stinson J., in his endorsement of July 30, 2007 approving the issuance of the DIP Approval Order, recorded the requests on behalf of the Superintendent and the USW that he record their respective clients' reservation of rights in relation to the pension fund payment and other matters referenced in paragraphs 6(a), 11(b) and (d) and paragraph 26 of the Initial Order. Since this reservation was recorded at the same time as the DIP Approval Order was granted and without any order being granted at that time to deal with any variations to the Initial Order, this raises a question of whether it is fair to regard the motion now before the Court as a collateral attack on the DIP Approval Order.

97 It is important that, in the Initial Order at paragraph 34, the DIP Facility was ordered to be on the terms and conditions in the DIP Term Sheet and Commitment Letter dated as of July 18, 2007 which was approved in that paragraph subject to a further hearing on the Comeback Date. Covenant No. 1 in the DIP Term Sheet and Commitment Letter provides that the Borrower shall not without the Lender's prior written consent make any material disbursement unless it is contemplated in the initial cash

flow or any subsequent cash flow approved by the Lender.

98 As noted earlier, on the motion to approve the Initial Order the Court had affidavit information from Automotive that the DIP Loan does not provide for the funding of any special payments, along with a copy of the cash flow which states that no provision is made for the payment of any special pension payments.

99 So, based on the above analysis, the Court, in the Initial Order, by reason of paragraph 34 (as to which no reservation of a right to object has been made or is now asserted), has ordered that the DIP Loan is not to be applied to special payments except with the consent of the DIP Lender.

100 The Superintendent seeks an order requiring the Applicant to pay the Special Payments. For the reasons given above, such an order would constitute a collateral attack on DIP Approval because the evidence is that the Applicant has no funds available to it other than the DIP Loan. Consequently, the order the Superintendent requests would effectively order the Applicant to use the DIP Loan for a purpose which, pursuant to paragraph 34 of the Initial Order, is not permitted.

101 Chrysler's agreement to act as DIP lender is based on the fact that the Applicant's supply is required to maintain Chrysler's own just-in-time vehicle manufacturing operations. The Superintendent submits that if Chrysler has concluded that it requires the output derived from the labour of the employees, then it is only fair and equitable that Chrysler bears the cost, in terms of remuneration to the employees including special payments to the Pension Plans, of that labour.

102 In the decision in *Ivaco Inc., Re* (2005), 47 C.C.P.B. 62 (Ont. S.C.J. [Commercial List]) at paragraph 4 (affirmed (2006), 275 D.L.R. (4th) 132 (Ont. C.A.), leave to appeal granted [2006] S.C.C.A. No. 490 (S.C.C.)) at the first instance, Farley J. characterized the nature of special payments, stating that "notwithstanding that past service contributions could be characterized as functionally a pre-filing obligation, legally the obligation pursuant to the applicable pension legislation is a 'fresh' obligation".

103 The amount of the outstanding special payments in the present case appears to have been determined prior to the Initial Order based on information relating to the pre-filing period. It is not apparent that the continuation of the operations of the Applicant in the post-filing period has given rise to an increase in the amount of the special payments from the amount that would otherwise have been applicable by reason of the pre-filing experience. Consequently, it seems tendentious to characterize the outstanding special payments as the costs of operating in the post-filing period.

104 The Superintendent objects that the approach that has been taken by the Applicant in the present case has been done without the requisite negotiation with the Superintendent and the pension plan stakeholders. In the decision in *United Airlines Inc.*, *supra*, Farley J. cited the example of a case where the company obtained specific relief from the requirement to make special payments although current service costs were made. The Court, however, concluded that such an arrangement "is not a 'given right' of the company" and is to be achieved "on a consensual basis after negotiation" with the pension plan stakeholders.

105 If there had been an objection to paragraph 34 of the Initial Order, that might well have occasioned negotiations of this kind, but there was no such objection. As noted, if there had been, each side could have assessed its own interests *vis-à-vis* the position of the other and the extent to which it would take the risk of insisting on its position or instead seek a compromise. Instead, what has happened is that the DIP Facility has proceeded without objection and the DIP Lender has changed its position on the basis of the Court orders given to date and now, after it has done so, an effort is made to put it in a position where it has no choice but to increase its funding or risk the loss of the continuing operations. This might yield a negotiation but it would be a lopsided one by reason of the DIP Lender already having provided funding in accordance with the Court orders.

106 The USW contends that its submissions in respect of paragraph 6 of the Initial Order are not in conflict with paragraph 34 because they do not seek an order that the DIP Lender provide the funds that Automotive would require to make the special payments or that Automotive make the payments, but only that it not be ordered that Automotive is not required to make those payments.

107 Since the material before the Court is to the effect that Automotive had and has no funds and has no expectation of having funds available which could be used to make the special payments, other than the monies available under the DIP Facility, if the Court were now to countenance and make the amendment to paragraph 6 which the moving party seeks, the necessary practical consequence of that amendment would be to allow pressure to be put on the DIP Lender to increase its funding commitment to Automotive and consent to Automotive making the special payments, because Automotive would otherwise be potentially vulnerable to proceedings to force it to meet its payment obligations and there would inevitably be concerns about the consequences that could flow from default on its part. That situation would be contrary to the expectations which both Automotive and the DIP Lender would reasonably have been entitled to hold in respect of the Initial Order. It might well be different if the moving party had instead sought an order that the "not required" clause in paragraph 6 should be subject to a proviso that it would not apply to the extent that payment of such amounts could be funded out of monies other than from the DIP Facility. There is no alternative request for such a proviso, perhaps because no one expects it would be of any use.

108 So what remains is a request that the Court, in the exercise of its discretion under s. 11, should make an order that would be contrary to the reasonable expectations of the Applicant and the DIP Lender based on the steps already taken and the orders already granted under the CCAA in this proceeding. That would be unfair and it would not contribute to the fair application of the CCAA in this case or as a precedent for others.

109 Moreover, the failure of the moving parties to reserve in respect of and then dispute paragraph 34 of the Initial Order has the following unsatisfactory effect. If the moving parties had duly disputed paragraph 34 there would have been an opportunity for the Court to consider what would have been the two opposing positions on whether the DIP terms proposed by the DIP Lender should be accepted. If that question had properly been put in issue, then there would also have been an opportunity for each side to consider whether it would seek to press its position or would compromise for the sake of the respective potential benefits to each side. No such opportunity would exists with the request that is now before the Court. So the request should not be granted.

110 For the reasons given above, there is no fair way at the present time to put the parties on a level playing field for negotiation about the special payments. For the reasons mentioned at other points above, it is desirable to ensure that there is an opportunity for such negotiation in CCAA circumstances, as an important means of achieving the most satisfactory arrangements for all concerned to the extent possible. With these considerations in mind, it is appropriate to take into account that the period of the application of the Initial Order was extended by Court order and will expire on the date set by the last such Order unless further extended. If a motion is made for a further extension of the Initial Order beyond its present expiry date, there would seem to be no basis in the above reasons to object to the legitimacy of interested parties raising an objection to paragraph 6 at that time, provided they are also prepared to object to paragraph 34.

Paragraph 11

111 The objection taken by the USW is that the provisions of s. 11 are open to an interpretation that would permit Automotive to repudiate its collective agreements with the USW's members.

112 Paragraph 11 is stated to be subject to covenants in the Definitive Documents as defined in the Initial Order. (They appear to be certain security documents.) The provision does not state that the right to terminate is subject only to such covenants. No mention is made in paragraph 11 of other obligations to which the Applicant may or may not be subject.

113 The USW seeks to have the rights provided for in clauses (b) and (d) of paragraph 11 made subject to all applicable collective agreements and labour laws. Those rights can only be exercised by agreement with the affected employees or other counterparty or under a plan filed under the CCAA, failing which the matters are to be left to be dealt with in any plan of arrangement filed by the Applicant under the CCAA. Nothing in the provision purports to abrogate any applicable collective agreement or labour laws. No reason was advanced why the authorized bargaining agent could not withhold agreement to any proposed exercise of clause (b) or (d) and if Automotive then sought to deal further with the matter pursuant to the CCAA there