

CITATION: **CITATION:** The Trustees of the Labourers' Pension Fund of Central and Eastern
Canada v. Sin-Forest Corporation, 2015 ONSC 3161
COURT FILE NO.: CV-12-9667-00CL
DATE: 2015-06-12

SUPERIOR COURT OF JUSTICE - ONTARIO

RE: The Trustees of the Labourers' Pension Fund of Central and Eastern Canada, the Trustees of the International Union of Operating Engineers Local 793 Pension Plan for Operating Engineers in Ontario, Sjunde AP-Fonden, David Grant and Robert Wong, Plaintiffs

AND:

Sino-Forest Corporation, Ernst and Young LLP, BDO Limited (formerly known as BDO McCabe Lo Limited) Allen T.Y. Chan, W. Judson Martin, Kai Kat Poon, David J. Horsley, William E. Ardell, James P. Bowland, James M.E. Hyde, Edmund Mak, Simon Murray, Peter Wang, Garry J. West, Pöyry (Beijing) Consulting Company Limited, Credit Suisse Securities (Canada), Inc., TD Securities Inc., Dundee Securities Corporation, RBC Dominion Securities Inc., Scotia Capital Inc., CIBC World Markets Inc., Merrill Lynch Canada Inc., Canaccord Securities (USA) LLC and Merrill Lynch, Pierce, Fenner & Smith Incorporated (successor by merger to Bank of America Securities LLC), Defendants

BEFORE: Regional Senior Justice G.B. Morawetz

COUNSEL: *Mary Margaret Fox* and *Paul Emerson*, for the Applicant Chubb Insurance Company of Canada

Kirk Baert and *Jonathan Ptak*, for the Ad Hoc Committee of Purchasers of the Applicant Securities, including the Class Action Plaintiffs

Gary Luftsprung and *Sam Sasso*, for Travelers Insurance Company of Canada

David Vaillancourt, for BDO Limited

Sara Erskine and *Jason Beitchman*, for Allan Chan

Susan Friedman, for Kai Kat Poon

David Cherepacha, for Lloyds, London

HEARD: April 20, 2015

ENDORSEMENT

Introduction

[1] The moving party, Chubb Insurance Company of Canada (“Chubb”) seeks a declaration that all funds paid by it, including a \$1,330,296.59 overpayment in excess of its limits of liability (the “Overpayment”) constitute Loss under the Policies for all purposes, such that any amounts paid by Travelers Insurance Company of Canada (“Travelers”) to reimburse Chubb, to the extent of the Overpayment, reduce the limit of liability under the Travelers policy.

[2] The position of Chubb is supported by Kit Kat Poon, Travelers and Lloyds of London (“Lloyds”).

[3] The Ad Hoc Committee of Purchasers of the Applicants’ Securities, including the Class Action Plaintiffs (the “Plaintiffs”) oppose the relief sought.

[4] The opposition of the Plaintiffs centres around the amount of insurance proceeds that have been paid in respect of defence costs.

[5] The Plaintiffs take the position that the court cannot provide the declaration requested by Chubb based on what they view as an incomplete evidentiary record. The Plaintiffs submit that Chubb, and the remainder of the Insurance Tower must produce a full and detailed accounting of the monies spent to date such that the court may satisfy itself as to the reasonableness of the defence cost payments in deciding whether to provide court approval for same.

Facts and Argument

[6] ACE-INA (“ACE”) issued Policy No. DO 024464 (the “ACE Policy”) covering Sino-Forest Corporation (“Sino-Forest”), its subsidiaries (as defined in the Policies and hereinafter, with Sino-Forest, collectively “Sino-Forest”) and their directors and officers (“Insured Persons” and, with Sino-Forest, collectively, “Sino-Forest Insureds”). The ACE Policy bears a \$15 million Limit of Liability (the “ACE Limit”).

[7] Chubb issued first excess Policy No. 8209-4449 covering the Sino-Forest Insureds (the “Chubb Policy”). In accordance with its terms, coverage under the Chubb Policy is excess to that coverage afforded by the ACE Policy. The Chubb Policy bears a \$15 million Limit of Liability (the “Chubb Limit”).

[8] There are two further excess layers of coverage provided by Certain Underwriters at Lloyd’s, which issued second excess Policy No. CTFF0420 (the “Lloyds Policy”) and by Travelers, which issued third excess Policy No. 10181108 (the “Travelers Policy”). The Lloyds Policy and the Travelers Policy each bear a \$15 million Limit of Liability (the “Lloyds Limit” and “Travelers Limit” respectively, (all of the policies herein collectively the “Policies”)).

[9] Chubb contends that with certain exceptions not material to this motion, the Chubb Policy, the Lloyds Policy and the Travelers Policy follow form to the ACE Policy, meaning that they adopt and incorporate all of the Insuring Agreements, definitions, terms and conditions of the ACE Policy.

[10] In total, directors' and officers' liability policies covering the Sino-Forest Insureds afford, in accordance with their terms, Limits of Liabilities totalling Cdn. \$62 million as set out below:

| LEVEL | INSURER | POLICY NO. | LIMIT OF LIABILITY (\$Cdn.) |
|---------------|----------------|------------|--|
| Primary | ACE | DO 024464 | \$15 million |
| First Excess | Chubb | 8209-4449 | \$15 million excess \$15 million |
| Second Excess | Lloyd's London | XTFF0373 | \$15 million excess \$30 million |
| Third Excess | Travelers | 101811008 | \$15 million excess \$45 million |
| Side A Excess | ACE | as above | \$1 million (Independent Directors only) excess \$60 million |
| Side A Excess | Chubb | as above | \$1 million (Independent Directors only) excess \$60 million |

[11] All Policies and the insurers identified above are sometimes hereinafter referred to as the "Insurance Tower".

[12] The events giving rise to these proceedings against Sino-Forest occurred in June 2011. At that time, certain Sino-Forest Insureds requested coverage from ACE (the first layer of the Insurance Tower) for various claims made against them.

[13] By January 2014, ACE had paid out the ACE limit of \$15 million in respect of defence costs, thereby exhausting Sino-Forest's first layer of insurance.

[14] Since that time, Sino-Forest's second layer (the Chubb limit of \$15 million) has been exhausted (plus, the Overpayment), and its third layer (the Lloyds limit of \$15 million has been exhausted or nearly exhausted).

[15] The Plaintiffs calculate that approximately \$41 million has been paid out as defence costs from the Policies since the commencement of these proceedings and, of that amount, \$26 million has been paid out since January 2014, and approximately \$18 million of the total has been paid out since July 2014.

[16] The defined terms "Defence Costs and Loss" are relevant. These definitions read, as follows:

ACE Policy, Section III.D:

"Defense Costs means reasonable and necessary costs, charges, fees and expenses incurred by any Insured in defending Claims and the premium for appeal, attachment or similar bonds arising out of covered judgments, but with no obligation to furnish such bonds. Defense Costs do not include wages, salaries, fees or other compensation of the Insured Persons or Company employees" (hereinafter "Defence Costs").

ACE Policy, Section III.I:

“Loss means the damages, judgments, any award of pre-judgment and post-judgment interest, settlements and Defense Costs which the Insured becomes legally obligated to pay on account of any Claim first made against any Insured during the Policy Period or, if elected, the Extended Reporting Period, for Wrongful Acts to which this Policy applies. Loss does not include: ...” (hereinafter “Loss”).

[17] The limits of all Policies in the Insurance Tower are self-depleting, meaning that payment of Defence Costs reduces the Limit available under each.

[18] Defence Costs have been paid to the following defendants to the Ontario Class Action:

- a. Sino-Forest, represented by Bennett Jones LLP
- b. W. Judson Martin, Peter Wang, Edmund Mak and Simon Murray, represented by Bennett Jones LLP;
- c. Allan T.Y. Chan, previously represented by Miller Thomson LLP and now represented by Reuter Scargall Bennett LLP;
- d. Kai Kat Poon, represented by Davies LLP;
- e. David Horsley, represented by Wardle Daley Bernstein Bieber LLP; and
- f. F. William E. Ardell, James P. Bowland, James M.E. Hyde and Gary J. West, represented by Osler Hoskin & Harcourt.

[19] Counsel to Chubb submitted that accounts rendered by defence counsel retained by Sino-Forest Insureds and by experts and other professionals retained by the Sino-Forest Insureds, with ACE’s consent (hereinafter “Defence Accounts”) were presented to ACE, reviewed by ACE or its coverage counsel for compliance with ACE’s litigation management guidelines, and paid, to the extent of what ACE’s review confirmed, constituted loss under the ACE policy.

[20] By January 2014, ACE had paid out its limit in respect of Defence Accounts. By order dated July 23, 2014, approving the settlement made by Mr. David Horsley with the Plaintiffs in various securities class actions and with Sino-Forest litigation trustee (the “Horsley Settlement Approval Order” and the “Horsley Settlement”), the court declared that the ACE limit was reduced accordingly, which exhausted the ACE Policy. Upon exhaustion of the ACE Policy, the Chubb Policy was engaged.

[21] Section III of the Policy provides that loss has two components – settlement amounts (damages if a Claim is tried, both referred to as “Indemnity Payments”) and Defence Costs.

[22] The only Indemnity Payment made by Chubb was the \$5 million which Chubb contributed to the Horsley Settlement.

[23] Paragraph 24 of the Horsley Settlement Approval Order declares that the \$5 million (as well as all Defence Costs paid to that date by Chubb) constituted covered Loss and reduced the Chubb Limit for all purposes. All other amounts paid by Chubb since that date were in respect of Defence Costs.

[24] Counsel to Chubb contends that timing issues resulted in Chubb making the Overpayment. Further, payment of Defence Costs by Chubb involves two steps – assessment of covered loss and payment of covered Loss.

[25] In the first step, Defence Accounts are reviewed for compliance with Chubb’s Litigation Management Guidelines (the “Chubb Guidelines”). Chubb contends that this review is conducted by a separate unit known as the Litigation Cost Management Group (“LCMG”). Defence Accounts are sent to LCMG for review for compliance with the Chubb Guidelines. The LCMG then reports back to Chubb’s claims handler, indicating the amount payable as Covered Loss.

[26] The Overpayment occurred in the payment phase, resulting from Chubb’s internal processes.

[27] The fact that the Overpayment was made was not disputed. Rather, what is disputed, is the process by which Defence Costs have been paid and whether there should be a review of such Defence Costs.

[28] Chubb takes the position that the Accounts have already been reviewed in the manner set forth in the governing documents. They submit that the defined terms “Defence Costs” and “Loss” are clear and that it is the LCMG which is to conduct the review. The Policy provides that Defence Costs are to be reasonable in the circumstances. Chubb submits that it is one of the functions of the LCMG to review Accounts and to make the determination whether the Defence Costs are reasonable in the circumstances. Chubb contends that it is satisfied that all amounts paid by Chubb constituted covered Loss under the Chubb Policy and the Policies.

[29] Chubb submits that the Plaintiffs have no standing to oppose the requested relief, as the Plaintiffs are not parties to the Policy and they have no direct interest in the Policy. At most, the Plaintiffs have a contingent interest. Further, Chubb submits that defence counsel are retained by the insureds and that, effectively, the Plaintiffs, in opposing the requested relief, are attempting to rewrite the terms of the policy.

[30] In addition, Chubb submits that the contract documents provide that the Plaintiffs have no right of action against the insurer.

[31] In this particular case, the direct right of action against the insurers was provided to the Plaintiffs as a result of the negotiated terms of the CCAA Plan of Arrangement (the “Plan”).

[32] The direct right of action is set out in Section 2.4(c) of the Plan as follows:

[...] For greater certainty, the insurers agree and consent to a direct right of action against the insurers, or any of them, in favour of any plaintiff who or which has (a) negotiated a settlement of any Claim covered under any of the Insurance

Policies, which settlement has been consented to in writing by the insurers or such of them as may be required or (b) obtained a final judgment against one or more of SFC and/or the Directors or Officers which such plaintiff asserts, in whole or in part, represents Loss covered under the Insurance Policies, notwithstanding that such plaintiff is not a named insured under the Insurance Policies and that neither SFC nor the Directors or Officers are parties to such action [...]

[33] Chubb contends that the terms of the Plan do not provide that the Plaintiffs can rewrite the insurance contract or in any way deprive the insureds of legal representation.

[34] Chubb also contends that the Plaintiffs have no right to second guess decisions to retain defence counsel or to review the type of work that counsel have been engaged in on behalf of the insureds.

[35] Finally, in seeking the requested relief, Chubb contends that there is no reason to punish Chubb for what, in essence, is a clerical error.

[36] Counsel for Kai Kat Poon supports the position taken by Chubb, and that she was only present to raise concerns about the possible prejudice that would affect Mr. Poon if the accounts of his counsel were to be scrutinized in a public forum. The dockets, as counsel emphasized, are privileged.

[37] The Plaintiffs acknowledge that there were significant negotiations and compromise prior to the voting and the sanction of the Plan. The Plaintiffs agreed to limit recovery in respect of certain claims to the proceeds of the Policies. The Insurers agreed to pay any Loss payable under the Policies. The insurers also consented to a direct right of action against them by the Plaintiffs.

[38] Counsel, on behalf of the Plaintiffs, contends that the court has the jurisdiction, at common law and under the CCAA and the *Class Proceedings Act*, to supervise the expenditures of counsel billing the policies. Further, by asking the court for a declaration that the funds paid constitute Loss under the policies, Chubb has invoked the court's jurisdiction and supervisory role.

[39] The Plaintiffs contend that in order to provide the requested approval of Chubb's payments to defence counsel, the court must satisfy itself that the amounts paid out as Defence Costs are "reasonable and necessary costs, charges, fees and expenses incurred".

[40] Counsel further submits that the court's inquiry into determining whether Defence Costs are "reasonable and necessary" is analogous to the inquiry on the passing of a receiver's account and the same principles and procedure should be applied. Counsel cited *Bank of Nova Scotia v. Diemer*, 2014 ONCA 851 where the Court of Appeal held that "in proceedings supervised by the Court and particularly where the Court is asked to give its *imprimatur* to the legal fees requested for counsel by its court officer, the court must ensure that the compensation sought is indeed fair and reasonable".

[41] In essence, the Plaintiffs seek court review or supervision of Defence Costs as such costs are currently \$41 million since the commencement of the proceedings. The Plaintiffs are of the view that much unnecessary time was spent opposing the Plaintiffs motion for certification and

leave, and opposing counsel needlessly attended cross-examinations and case conferences where their clients had little or no interest at stake.

[42] The Plaintiffs are of the view that in order to determine whether the amounts paid out as Defence Costs are “reasonable and necessary”, the court requires an evidentiary record on which to base that conclusion and, at a minimum, the motion should be adjourned, and the remainder of the Insurance Tower, be required to provide a full and detailed accounting of the amounts paid out to date in respect of Defence Costs.

Analysis

[43] There is no doubt that the amount paid on account of Defence Costs has had a significant impact on the proceedings but, in my view, in the circumstances of this case, it does not fall to the court to supervise and review the amounts paid for Defence Costs. I reach this conclusion for the following reasons:

1. The Policies are contracts as between the insurer and the insureds.
2. Apart from the applicable provisions in the Plan, the Plaintiffs have no direct right of action against the insurer.
3. The direct right of action was provided to the Plaintiffs as a result of the Plan of Arrangement (section 2.4).
4. The Sino-Forest Insureds are entitled to have representation in defending claims. Defence Costs are paid by the insurer. Defence Costs have to be reasonable in the circumstances and payment of Defence Costs are administered through the Chubb Guidelines. LCMG has reviewed the Defence Costs.
5. During the investigation of a claim, the Plaintiffs have no say in the manner in which the claim is being defended.

[44] At no time did the Plaintiffs negotiate for or obtain the right to review the accounts.

[45] In essence, the Plaintiffs are asking the court to rewrite the insurance contract so as to provide them with additional rights.

[46] The Plaintiffs have released a number of potential defendants and have agreed to limit recovery in respect of certain claims to the proceeds of the Policies. These were decisions made by the Plaintiffs. The Plaintiffs had it within their control to raise the issue of Defence Costs in the context of and as part negotiation of section 2.4 of the Plan. They could have insisted on language which would give the court the supervisory power to review the accounts. They did not negotiate for that right.

[47] With respect to the directors and officers who have not been released, it is not appropriate, in my view, for the court to review or restrict the type of defence that these defendants wish to mount.

[48] The reliance that the Plaintiffs put on the *Diemer* case is, in my view, misguided. *Diemer* involved a court appointed receivership. In *Diemer*, by court order, the court was required approve the fees of the receiver and its counsel. The receiver is a court officer. There is no corresponding provision in the Plan or in any order in the CCAA proceedings that requires the court to review or approve Defence Costs in the manner suggested by the Plaintiffs.

[49] In my view, it is not appropriate for the court to intervene and to supervise the accounts of defence counsel. Such intervention could have a very detrimental effect on the rights of the remaining insureds to mount the type of defence that they wish to do so.

[50] While I recognize that the Defence Costs in these proceedings are significant, the contractual documents are clear. The mechanism for controlling the Defence Costs is provided for in the Policies. The Plaintiffs did acquire certain rights as a result of the negotiation of the Plan. Had they wished to obtain a degree of direct or indirect supervision of Defence Costs, the same should have been provided for at the time the Plan was negotiated, not now.

Disposition

[51] The position of Chubb prevails.

[52] In light of my conclusion, in my view, it is not necessary to delve into the issue raised by Chubb of whether the Plaintiffs have standing to oppose the requested relief.

[53] In the result, the requested declaration shall issue that the funds paid out by Chubb out of the Chubb Policy as detailed in the affidavit of Ms. Kargas, constitute Loss that reduces the limit of liability under the Chubb Policy, for all purposes. An order shall issue authorizing Travelers to reimburse Chubb to the extent of the Overpayment. A declaration shall also issue that Travelers' reimbursement of the overpayment to Chubb constitutes a Loss that reduces the limit of liability under the Travelers policy. Finally, all persons provided with notice of this Motion, including all Sino-Forest Insureds, are bound by the foregoing declarations.

[54] Costs in the agreed upon amount of \$20,000 are awarded in favour of Chubb and the parties that supported Chubb.



Regional Senior Justice Morawetz

Date: June 12, 2015