File No. CI20-01-26627

THE QUEEN'S BENCH
Winnipeg Centre

IN THE MATTER OF: THE APPOINTMENT OF A RECEIVER PURSUANT TO SECTION 243 OF THE BANKRUPTCY AND INSOLVENCY ACT, R.S.C., C.B-3, AS AMENDED, AND SECTION 55 OF THE COURT OF QUEEN'S BENCH ACT, C.C.S.M., C.C280, AS AMENDED

BETWEEN:

WHITE OAK COMMERCIAL FINANCE, LLC.

Applicant

- and -

NYGARD HOLDINGS (USA) LIMITED, NYGARD INC., FASHION VENTURES, INC., NYGARD NY RETAIL, LLC., 4093879 CANADA LTD., 4093887 CANADA LTD., NYGARD INTERNATIONAL PARTNERSHIP, NYGARD PROPERTIES LTD., and NYGARD ENTERPRISES LTD.

Respondents

AND

Estate Nos: 31-2627758, 31-2627760, 31-2627764, 31-2627767, and 31-458926
IN THE MATTER OF THE NOTICE OF INTENTION TO FILE A PROPOSAL OF NYGARD PROPERTIES LTD., NYGARD ENTERPRISES LTD., NYGARD INTERNATIONAL PARTNERSHIP, 4093879 CANADA LTD., AND 4093887 CANADA LTD.

MOTION BRIEF OF THE RESPONDENTS

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File No. 113885/WMO

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MOTION BRIEF OF THE RESPONDENTS

INDEX

PART I - AUTHORITIES **TAB**

PART II – POINTS TO BE ARGUED

1. This brief is filed in addition to the previous briefs filed by the Respondents in this matter. The Respondents repeat and rely upon the arguments set out in its previous briefs.

2. It is agreed amongst the parties that Nygard Property Ltd. (NPL) is entitled to be represented by counsel. If this were not the case the Court would be put in the difficult position of having only the Receiver's materials and having to examine the thousands of pages of exhibits, like the credit agreements and debentures, without the help of expert experienced insolvency counsel. The issues in this case are both complex and, in some instances, novel.

3. It is not in question that counsel acting for the companies involved in the Receivership can have access to the money that remains in the Levene Taman Golub trust account in the amount of $200,000 in accordance with the agreement entered into by the parties and approved by this court.

4. One question to be answered by the court is can those same lawyers have access to money (approximately $10,000,000) that is currently in the possession of the Receiver as a result of the sale of the assets of the companies that have been part of the receivership? It is the position of NPL the answer is yes.

5. A second question to be answered by the court is can lawyers involved in the defence of criminal charges against Peter Nygard have access to either the $200,000 remaining in the Levene Tadman Golub trust account or the $10,000,000 in the Receivers account? Once again it is the position of NPL the answer is yes.

PART III – FACTS

6. To state the obvious, the insolvency litigation is ongoing, and once this court issues its judgement there may be appeals and further litigation.

7. Nygard Enterprises Ltd. (NEL) is owned by Peter Nygard. NEL owns NPL.

8. If Peter Nygard is convicted of one or more of the criminal charges he faces, the aggrieved parties will file or will continue to prosecute their civil claims and it is unlikely Mr. Nygard will have a viable defence having been found guilty with the legal test of beyond a reasonable doubt. Once a judgment is obtained, these parties will be able to seize the shares in NEL and ultimately the assets of NPL.

9. Currently there is no evidence before this Court that would allow this Court to come to a determination that Mr. Nygard did anything wrong while working for NPL or otherwise.

10. If Mr. Nygard is acquitted NPL will have a series of defences it can rely on, including testimony from Peter Nygard, which would allow them to defend a civil claim in a meaningful way.

11. NPL's other creditor, Canada Revenue Agency (CRA), is being satisfied by NPL's agreement to have the Receiver hold monies which might otherwise be payable to CRA.

12. The inter-company debts may not be enforceable because of the credit agreement entered into with White Oak as was previously argued.

13. The creditors of Nygard International Partnership (NIP) did not bargain that NPL would guarantee monies payable by NIP. The NIP creditors had not asked for a guarantee and should not be given one now.

14. The breakdown of the $1,150,000.00 request is: Criminal lawyers - $350,000.00 to Brian Greenspan; $50,000.00 to Jeff Hartman; $50,000.00 to Richard Wolson; $50,000.00 to Jay Prober for a total of $500,000.00. Insolvency lawyers - $250.000.00 to Fred Tayar and Associates; $350,000.00 to Levene Tadman; $50,000.00 to Albert Gelman Inc.

15. With respect to Levene Tadman the current indebtedness after the payment of the $150,000.00 in this Court's Order of December 22nd, 2021, is approximately $50,000.00.

16. With respect to Fred Tayar and Associates the current indebtedness is approximately $31,000.00.

17. There is now approximately $200,000.00 remaining in the Levene Tadman Trust Account from the sale of the Fieldstone property in Toronto.

PART IV – ARGUMENT

18. The Receiver takes three positions. First, NPL has not established a right to the monies currently in the possession of the Receiver (this being distinct from the $200,000.00 currently in the Levene Tadman Golub Trust Account). Any decision the Court would make with respect to the monies in the Receiver's possession must be made keeping in mind NPL still needs to fund its lawyers so that it can argue any appeal or defend any appeal from the decision of the Court in 2022. Even if NPL does not have a right to the monies in the Receiver's hands, it does have a right to have money so that it can argue its position;

19. In regard to the Receiver's argument, the Respondents point to *The Annotated Bankruptcy and Insolvency Act*, Houlden, Morawetz & Sarra, 4th Edition, at § 3:62. [**Tab 1**]), where the authors say:

> If an interim receiver has been appointed, the court, if it deems it appropriate, may authorize an advance by the interim receiver out of the debtor's assets to pay the legal costs of defending the application: *Re King Petroleum Ltd.* (1973), 18 C.B.R. (N.S.) 270 (Ont. S.C.). The defence must not be frivolous or vexatious: *Royal Bank v West-Can Resources Finance Corp.* (1990), 3 C.B.R. (3d) 55, 1990 CarswellAlta (Q.B.)…

20. In *Re King Petroleum Ltd.* (1973), 18 C.B.R. (N.S.) 270 (Ont. S.C.) [**Tab 2**], an interim receiver was appointed at the behest of a petitioning creditor. The debtor disputed the petition in bankruptcy and asked the interim receiver to pay its lawyers to appear on the return of the petition to present the debtor's position on the dispute. The Registrar, after pointing out that every case will depend on its own particular facts, found that "the interim

receiver should make funds available to counsel for the debtor, so that the debtor can put forth its defence as may be advised." The Court noted that the right to put forth a defence would be hollow without the ability to pay legal counsel.

21. Additionally, in *Royal Bank v West-Can Resource Finance Corp.*, 1990 CarswellAlta 239 (AB QB) [**Tab 3**], the bank held a debenture which provided that its remedy in the case of default was to apply to the court for the appointment of a receiver. The bank issued a statement of claim against the debtor and applied for the appointment of a receiver. The debtor contended that the Court should authorize the receiver to pay the legal fees incurred by the debtor in defending the action and counterclaiming. The Court agreed, holding that the receiver was authorized to pay the debtor's legal fees. The defence was known at law, and neither the defence nor the counterclaim were frivolous or vexatious. Further, the Court echoed the comments in *Re King Petroleum* that the right to raise a defence would be empty if effective presentation of the defence could not be paid for from the debtor's resources.

22. The Respondents submit that they need to be able to put forth their defence and that same is neither frivolous or vexatious.

23. The second position taken by the Receiver is that NPL should not use its money to pay criminal lawyers for Peter Nygard because its interests are distinct from that of Peter Nygard. It is the position of NPL that because Peter Nygard is the ultimate owner of NPL, it is in NPL's best interests that Peter Nygard be acquitted. If Peter Nygard is convicted, NPL's assets would likely be used to pay a judgment obtained by anyone who is successful in the prosecution of a civil claim after a successful criminal prosecution against Peter

Nygard. Further, NPL may be added to the criminal proceedings and the work done in defence of Mr. Nygard could be useful to NPL (see: Affidavit of Brian Greenspan, affirmed December 9, 2021, at paragraph 5).

24. The third position taken by the Receiver is that NPL cannot make a payment because of sections 113, 117 and 119 of *The Manitoba Corporations Act*, CCSM c C225 [**Tab 4**]. Those sections describe instances when a corporation can pay the legal costs of an officer, director or employee. Mr. Nygard is not currently an officer, director or employee of NPL so it is not on this basis that NPL is suggesting monies should be paid on his behalf. Mr. Nygard was an officer of NPL. When he was, his position is his conduct was in accordance with the company's scope for his work and certainly not criminal. The company is unaware of any conduct that was not within the scope of his employment or criminal. There is not evidence before this Court to the contrary.

25. In the event section 119 of the *Corporations Act* is applicable, the leading Manitoba case on the indemnification provisions is *Manitoba (Securities Commission) v Crocus Investments Fund*, 2007 MBCA 36 ["*Crocus*"] [**Tab 5**]. In *Crocus*, the Manitoba Court of Appeal applied the test set out by the Supreme Court of Canada in *Blair v Consolidated Enfield Corp.*, [1995] 4 SCR 5 (SCC) ["*Blair*"]:

> [36] Iacobucci J. then identified the three conditions that must exist "in order to receive indemnification for the costs of defending in litigation" (at para. 36):
>
> 1. the person must have been made a party to the litigation by reason of being a director or an officer of the corporation;

2. the costs must have been reasonably incurred; and

3. the person must have acted honestly and in good faith with a view to promoting the best interests of the corporation.

26. The Respondents submit that for the above reasons, all three conditions have been met.

27. In considering the third requirement, there is a presumption that the party seeking indemnification acted in good faith and had reasonable grounds to believe their conduct was lawful. In *Crocus*, the Court of Appeal cited *Blair* on the issue of good faith:

> [35] … [P]ersons are assumed to act in good faith unless proven otherwise… a proper construction of the statute and law related to good faith issues reveals that Blair is not required to prove his good faith… To a large extent, it is the corporation that must establish, to the satisfaction of the court, exactly what Blair did that was inimical to its best interests.
>
> [*Emphasis Added*]

28. In *Bennett v Bennett Environmental Inc.*, 2009 ONCA 198 ["*Bennett*"] [**Tab 6**], the Ontario Court of Appeal considered the equivalent indemnification provisions under the *Canada Business Corporations Act*, RSC 1985, c C-44. In *Bennett*, the company, the CEO/Chair-person, and other directors were subject to a class action and securities and criminal proceedings in the United States and Ontario. The applicant CEO and Chair-person sought indemnification from the company but the company refused. The applicant

brought an application for a declaration that he was entitled to indemnification for all proceedings. The application judge held that the company failed to establish that the applicant did not satisfy the requirements of s 124(3) of the *Canada Business Corporations Act* and the company was ordered to indemnify the applicant. The company appealed and the ONCA dismissed the appeal.

29. In their discussion on the requirement that the individual reasonably believe that their conduct was lawful, the Ontario Court of Appeal in *Bennett* said the following:

> [32] … the corporation also bears the burden of showing that the director did not have reasonable grounds for his or her belief that the conduct was lawful… In my view, under s. 124(3)(b), persons should also be assumed to believe they are acting lawfully and to have reasonable grounds for that belief, unless the contrary is proven…
>
> [*Emphasis Added*]

30. At paragraph 18 of the Receiver's Supplemental Motion Brief, filed December 29, 2021, the Receiver argues that Mr. Nygard could not have been acting in good faith and that Mr. Nygard could not have possessed a reasonable belief that his conduct was lawful. However, the Receiver does not go beyond referencing the charges and the nature of the charges. In *Crocus*, the Manitoba Court of Appeal made it clear that more is required to rebut the relevant presumptions:

> [40] … Allegations in pleadings or by the Manitoba Securities Commission, or the extra-judicial conclusions of the Auditor General, are not evidence, and

cannot, unless and until they are established in a legal proceeding, displace the presumption of good faith which is well recognized at law.

31. The Receiver has not introduced evidence sufficient to establish that Mr. Nygard acted in bad faith or lacked reasonable grounds to believe his conduct was lawful.

32. Based on the foregoing, the Respondents submit that their Notice of Motion, dated December 10, 2021, should be granted.

ALL OF WHICH IS RESPECTFULLY SUBMITTED THIS 5th DAY OF JANUARY, 2022.

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§ 3:62. Advancing Funds to the Debtor to Pay Costs of Defending Application

See § 8:123 “Legal Costs Preceding the Assignment or Application and in Connection with the Assignment or Application”.

If an interim receiver has been appointed, the court, if it deems it appropriate, may authorize an advance by the interim receiver out of the debtor's assets to pay the legal costs of defending the application: Re King Petroleum Ltd. (1973), 18 C.B.R. (N.S.) 270 (Ont.S.C.). The defence must not be frivolous or vexatious: Royal Bank v. West-Can. Resources Finance Corp. (1990), 3 C.B.R. (3d) 55, 77 Alta. L.R. (2d) 43, 1990 CarswellAlta 239 (Q.B.). The amount of such advance will be whatever the court considers reasonable, balancing the interests of the debtor in defending the application and the interests of creditors in preserving the assets for their benefit: Re C.J. Wilkinson Ford Mercury Sales Ltd. (1986), 60 C.B.R. (N.S.) 318, 1986 CarswellOnt 214 (Ont. S.C.). If an interim receiver has had to borrow in order to carry on the business of the debtor, the court will not order the payment of an advance to defend the application: Re Inter. Chemalloy Corp. (1975), 19 C.B.R. (N.S.) 299 (Ont. Reg.).
Where the ownership of funds in the possession of an interim receiver was uncertain, the court refused to order the interim receiver to advance funds to the debtor to defend an application: Newell v. McIvor (1997), 47 C.B.R. (3d) 300, 157 Sask. R. 12, 1997 CarswellSask 405 (Q.B.).

The Ontario Court of Appeal considered, once default judgment has been granted, under what conditions can a defendant's funds paid into court pursuant to a Mareva injunction be paid out to the defendant for legal fees and reasonable legal expenses. The four-part test on a motion by a defendant for payment out of monies held under a Mareva injunction for legal and living expenses are: 1) has the defendant established that he or she has no other assets available to pay expenses other than those frozen by the injunction? 2) if so, has the defendant shown that there are assets caught by the injunction that are from a source other than the plaintiff, *i.e.* assets that are subject to a Mareva injunction, but not a proprietary claim, 3) the defendant is entitled to the use of nonproprietary assets frozen by the Mareva injunction to pay reasonable living expenses, debts and legal costs, those assets must be exhausted before the defendant is entitled to look to the assets subject to the proprietary claim; and 4) if the defendant has met the previous three tests and still requires funds, the court must balance the competing interests of the plaintiff in not permitting the defendant to use the plaintiffs money for his or her own purposes and of the defendant ensuring a proper opportunity to present a defence before assets in his or her name are removed from him or

her without a trial. Here, Feldman J.A. found that although the appellant claimed that he intended to move to set aside the default judgment, no motion had been brought, nor had any statement of defence been delivered, and on the basis of the record before the court, there appeared to be no defence available to the appellant on the merits. In such circumstances, Feldman J.A. held that there was no principled reason for the appellant to be able to deplete the funds in court which were subject to the judgment and available to judgment creditors: B & M Handelman Investments Ltd. v. Curreri (2011), 2011 CarswellOnt 3436, 2011 ONCA 395 (Ont. C.A.).

Footnotes

*

[am 2004, c. 25, s. 26]

1973 CarswellOnt 87
Ontario Supreme Court, In Bankruptcy

King Petroleum Ltd., Re (No. 2)

1973 CarswellOnt 87, [1973] O.J. No. 1324, 18 C.B.R. (N.S.) 270

Re King Petroleum Limited

J. M. Ferron, Q.C., Registrar

Judgment: September 27, 1973

Counsel: *C. H. Morawetz, Q.C.*, for King Petroleum Limited.
J. C. Osborne, for interim receiver and creditor.

Subject: Corporate and Commercial; Insolvency
Related Abridgment Classifications
Bankruptcy and insolvency
IV Receivers
IV.3 Powers, duties and liabilities
Headnote
Bankruptcy --- Interim receiver — Powers, duties and liabilities
Interim receiver — Controlling disbursements — Retainer to solicitors defending petition for receiving order.
The interim receiver has fixed and special duties to perform under the direction of the court, and he is responsible to the court and not the petitioning creditor. As an officer of the court, it is essential that where required, the interim receiver should retain independent counsel so there can be no question of his independence with respect to the petitioning creditor. Under an interim receiving order the interim receiver is directed to control disbursements. However, by reason of the control of the disbursements the debtor should not be put in an embarrassing position by reason of the lack of funds where those funds are required for a legitimate purpose. The question of what is a legitimate purpose must be decided in every case on the particular facts before the court. Where it appeared that several issues had to be tried of some complexity, *held*, under the circumstances, the interim receiver should make funds available to the solicitor for the debtor, so that the debtor could put forth its defence as may be advised. An order was made authorizing the interim receiver to put the solicitors for the debtor in funds to the extent of $10,000 as a retainer to be accounted for by the said solicitors and subject to any further order made by the court on the final determination of the issue.
Annotation

In this case, the interim receiver and the Court were faced with a difficult problem. The debtor should be entitled to defend the petition and be allowed sufficient funds to provide for this. However, if the debtor is insolvent and a receiving order is made, the funds used to defend the petition would have been available for distribution among the creditors. This is a situation which could lead to very serious abuse and must be scrutinized by the court very carefully. The court must be very alert to prevent funds available to creditors being dissipated by frivolous and vexatious proceedings. The Registrar acknowledged that each case must be determined on its own facts. In this particular case, the Registrar found that the amount involved, the acts of bankruptcies set out in the petition and the nature of the dispute filed justified the payment of the retainer.

***Ferron*, Registrar:**

1 A petition for a receiving order was issued on 17th July 1973, by Imperial Oil Limited against King Petroleum Limited alleging an indebtedness of $705,293.91 for goods sold and delivered. On that same day, I made an order appointing The Clarkson Company Limited as interim receiver and directed the interim receiver to take immediate possession of the property of King Petroleum Limited and to control the receipts and disbursements of that company.

2 A dispute to the petition was filed on behalf of King Petroleum on 5th September 1973. The matter came up before Houlden J. on 6th September 1973, at which time an order was made permitting counsel for King Petroleum Limited to cross-examine on the affidavit of verification filed by the petitioning creditor.

3 It appears from the affidavit of Ronald A. McKinlay, vice-president of the interim receiver that at the request of counsel acting for King Petroleum Limited, a cheque in the amount of $10,000 was issued by the interim receiver to be a retainer for the solicitors for King Petroleum Limited who were acting for King Petroleum Limited in disputing the petition. Mr. McKinlay states in para. 4 of his affidavit, "subsequent to the arrangement being made, but before the ten thousand dollar cheque cleared the King Petroleum Limited bank account, the Interim Receiver was advised by its counsel, Messrs. MacMillan, Binch that the arrangement was improper and accordingly payment of the ten thousand dollar cheque was stopped by the Interim Receiver".

4 This application accordingly is for an order authorizing the interim receiver to issue a cheque to counsel for King Petroleum as a retainer in connection with the defence of the petition. It is clear that unless funds are made available to King Petroleum the defence of the petition will be prejudiced.

5 It is argued by counsel for the interim receiver who is also counsel for the petitioning creditor that the dispute filed by King Petroleum Limited is frivolous and that the retainer requested is excessive. The merits of the dispute filed, obviously cannot be dealt with at this time and even if the dispute were on its face manifestly without merit there will be no jurisdiction in the Registrar to deal with that situation. Accordingly, that argument cannot be taken into consideration on this application.

6 King Petroleum Limited, having filed a dispute has the right to put forth its defence but this would be a hollow right if funds were not forthcoming to permit the respondent to engage counsel to advance its position.

7 It would seem that the interim receiver appreciated this position, since arrangements were made to put the debtor in funds to enable it to engage legal counsel. The cheque for the retainer was, as I have mentioned above, issued but payment of the cheque was stopped on the advice of the interim receiver's solicitors. I have no doubt that this advice was motivated on proper considerations, but one can see the dangers of possible bias where the interim receiver and petitioning creditor are represented by the same counsel. The interim receiver has fixed and special duties to perform under the direction of the court, and he is responsible to the court and not the petitioning creditor. As an officer of the court, it is essential that where required, the interim receiver should retain independent counsel so there can be no question of his independence with respect to the petitioning creditor.

8 Under the interim receiving order made on 17th July 1973, the interim receiver was directed to control disbursements. It is quite clear that by reason of the control of the disbursements the debtor should not be put in an embarrassing position by reason of the lack of funds where those funds are required for a legitimate purpose. The question of what is a legitimate purpose must be decided in every case on the particular facts before the court. In this particular instance it appears from the amount involved, the acts of bankruptcy set out in the petition and a general perusal of the dispute that there are several issues to be tried of some complexity. As mentioned above, the matter came before Houlden J. on 6th September and the order was made as I have mentioned above and trial fixed for 12th and 13th November next. I am of the opinion that, under the circumstances, the interim receiver should make funds available to counsel for the debtor, so that the debtor can put forth its defence as may be advised.

9 On the application there was no material filed to indicate in what manner the figure of $10,000 as a retainer was determined. It appears however, from the interim receiver's affidavit and indeed from his action that he must have been convinced that the amount was reasonable. It would seem to me that on these applications some material should be filed to indicate the funds expected reasonably to be expended, so that there may be some basis by which to determine the quantum of retainer to be ordered.

10 In conclusion, an order will go authorizing the interim receiver to put the solicitors for King Petroleum Limited in funds to the extent of $10,000 as a retainer to be accounted for by the said solicitors and subject to any further order made by the court on the final determination of this issue. I think the costs should be reserved to be dealt with likewise on the final termination of this matter.

1973 CarswellOnt 87, [1973] O.J. No. 1324, 18 C.B.R. (N.S.) 270

End of Document

Most Negative Treatment: Distinguished
Most Recent Distinguished: Peterborough (City) v. Kawartha Native Housing Society Inc. | 2009 CarswellOnt 3478, 178 A.C.W.S. (3d) 116 | (Ont. S.C.J., Jun 17, 2009)

1990 CarswellAlta 239
Alberta Court of Queen's Bench

Royal Bank v. West-Can Resource Finance Corp.

1990 CarswellAlta 239, [1990] A.W.L.D. 813, 25 A.C.W.S. (3d) 1248, 3 C.B.R. (3d) 55, 77 Alta. L.R. (2d) 43

ROYAL BANK OF CANADA v. WEST-CAN RESOURCE FINANCE CORPORATION; WEST-CAN RESOURCE FINANCE CORPORATION v. ROYAL BANK OF CANADA

MacPherson J.

Judgment: June 19, 1990
Docket: Doc. Calgary 9001-06330

Counsel: *R.C. Dixon* and *J.S. Shortt*, for defendant (plaintiff-by-counterclaim).
B.P. O'Leary and *B.R. Crump*, for plaintiff (defendant-by-counterclaim).

Subject: Corporate and Commercial; Insolvency; Civil Practice and Procedure
Related Abridgment Classifications
Debtors and creditors
VII Receivers
VII.7 Actions involving receiver
VII.7.d Actions against debtor in receivership
Headnote
Receivers --- Actions by and against — Actions against debtor in receivership
Receivers — Duties and liability — Creditor commencing action against corporate debtor and obtaining order appointing receiver — Debtor having defence to action — Receiver authorized to pay legal fees incurred by debtor.
The bank held a debenture which provided that its remedy in the case of default was to apply to the Court for the appointment of a receiver. The bank issued a statement of claim against the debtor and applied for the appointment of a receiver. The debtor contended that the Court should authorize the receiver to pay the legal fees incurred by the debtor in defending the action and counterclaiming.
Held:
The receiver was authorized to pay the debtor's legal fees.
The defence was known at law, and neither the defence nor the counterclaim was frivolous or vexatious. The right to raise a defence would be empty if effective presentation of the defence could not be paid for from the debtor's resources. The order appointing the receiver was a preservation or custodial order. A court-appointed receiver has different duties from a contractually-appointed realizing receiver. While the bank would recover less if the debtor's suit were successful, this inequity resulted from the contract which the bank entered into with the debtor.
Table of Authorities
Cases considered:
Bank of Nova Scotia v. Dunphy Leasing Enterprises Ltd. (1990), 105 A.R. 161 (Q.B.) — *referred to*
King Petroleum Ltd., Re (1973), 18 C.B.R. (N.S.) 270 (Ont. S.C.) — *considered*
Newhart Developments Ltd. v. Co-operative Commercial Bank Ltd., [1978] Q.B. 814, [1978] 2 All E.R. 896 (C.A.) — *considered*

Toronto-Dominion Bank v. Fortin, 26 C.B.R. (N.S.) 168, [1978] 2 W.W.R. 761, 85 D.L.R. (3d) 111 (B.C. S.C.) — *referred to*

Statutes considered:

Interest Act, R.S.C. 1985, c. I-15.

APPLICATION to settle terms of order appointing receiver.

***MacPHERSON J.*:**

1 This is an application to settle one of the terms of an order that I have made in these proceedings.

2 The debtor was of the view that the Court should authorize the receiver to pay the legal fees incurred by the debtor in defending this action and prosecuting the counterclaim. The bank was of an opposite view.

3 It is important to recall the whole of the unique facts in this case to understand the equities involved that require consideration and need be addressed in the order.

4 The bank's debenture had no power to appoint a receiver and crystallize the floating charge. The debenture provided that the bank's remedy in the event of default was to apply to the Court for the appointment of a receiver. The bank issued a statement of claim and applied to the Court for the appointment of that receiver. The debtor defended the action and counterclaimed on the basis of the decision in *Bank of Nova Scotia v. Dunphy Leasing Enterprises Ltd.* (26 March 1990), Docs. Calgary 8201-14168, 8201-32649, 8201-32646 and 8801-03015, Power J. (Alta. Q.B.) [now reported at (1990), 105 A.R. 161], in which a defence based on the *Interest Act*, R.S.C. 1985, c. I-15, and miscalculation of, or misstatement of, interest was successful as against the bank.

5 The debtor says on a proper calculation of interest there remains no indebtedness to the bank. The bank says our books show a substantial outstanding indebtedness. The issue requires determination at trial.

6 On the motion the bank asked the Court to appoint a receiver, and the debtor asked that the bank be enjoined from enforcing its securities until the issue between the parties was resolved.

7 It is important to the whole of the deliberation that it be recognized that the bank chose to ask the Court to intervene rather than enforcing its various securities against the debtor's property. The Court must move in matters such as this in an impartial way, seeking to preserve the various rights and property of the litigants pending determination of the issues between them.

8 The order sought in this hearing is an integral part of the balancing of the competing equities sought to be achieved by the recent order that was made. It is only because this aspect of the order required careful argument and review that it was set down as a special application.

9 The argument of the bank is based on the decision in *Newhart Developments Ltd. v. Co-operative Commercial Bank Ltd.*, [1978] Q.B. 814, [1978] 2 All E.R. 896 (C.A.). Essentially, the bank says funding the defence and counterclaim out of the debtor's cash flow is taking that which is secured to the debenture holder. Further, the bank argues that it is unfair in that, if the bank loses at trial, the debtor can be compensated in damages and no one has any doubt that the bank has the ability to pay. If the debtor loses, the bank will simply have a greater shortfall in the recovery of the debt due to it.

10 The debtor says that the bank is in error. The *Newhart* decision is clearly distinguishable on its facts. In *Newhart*, the bank had put its receiver into possession by "private" appointment. Two years after the realization process was begun, the debtor company issued a writ suing the bank for breach of contract. The ratio of the case is that the debtor can sue as long as it does not take away from, or interfere with, the receiver's property in possession. One real distinction is that the receiver was a contractual receiver appointed by the bank to realize for the bank.

11 Another substantial distinction is that in *Newhart* the receiver was in possession, and the Court said you cannot take away that which he has, by contract, in his possession. In the case at Bar the shoe is on the other foot. The debenture provides there can be a receiver appointed, with the concomitant perfecting of the floating charge, but only if the Court orders it. The

allegedly secured creditor is seeking to take away from the debtor that which it has in its lawful possession without the secured creditor showing that it has the right so to do. Whatever else may be attributed to the drafters of this debenture agreement, the knowledge that the Court would not take away one's property until the right to do so had been proven must be considered to be at least within the reasonable expectation of the parties.

12 In the case at Bar, the order is a preservation custodial-type order appointing a receiver. That receiver has a different duty than the realizing contractually appointed receiver.

13 *Kerr on Receivers* [Raymond Walton, *Kerr on the Law and Practice as to Receivers*], 15th ed. (London: Sweet & Maxwell, 1978), at p. 7, where the learned author states:

> The duty of the court upon a motion for a receiver is merely to protect the property for the benefit of the person or persons to whom the court, when it has all of the materials necessary for a determination, shall think it properly belongs.

14 The debtor relies heavily on the much referred to judgment of Anderson J. of the British Columbia Supreme Court in *Toronto-Dominion Bank v. Fortin*, 26 C.B.R. (N.S.) 168, [1978] 2 W.W.R. 761, 85 D.L.R. (3d) 111. While that judgment points out that the company has the right to raise its defences, and it is not for the receiver to decide whether or not the defences should be raised, the case does not say who will pay for those defences.

15 The debtor says that if the right to raise the defences lies with the company, surely it is a necessary ancillary to this principle that the debtor be allowed to pay for the defences, otherwise it will have no right at all.

16 The debtor suggests that this principle is enunciated in *Re King Petroleum Ltd.* (1973), 18 C.B.R. (N.S.) 270 (Ont. S.C.). The case is to some degree analogous, but not on all fours. In that case, an interim receiver was appointed at the behest of a petitioning creditor. The debtor disputed the petition in bankruptcy and asked the interim receiver to pay its lawyers to appear on the return of the petition to present the debtor's position on the dispute. The contest was not between a secured creditor and the debtor, but between the creditors who were claiming the funds and the debtor. In that case, the learned Registrar, after pointing out that every case was dependent on its own particular facts, found [at p. 272] that "the interim receiver should make funds available to counsel for the debtor, so that the debtor can put forth its defence as may be advised."

17 That case and cases that followed it provided that it would be an empty right to raise a defence if effective presentation of the defence could not be paid for in a practical way from the debtor's resources.

18 Here, the funds required are for a defence known at law. I have held that it is not a frivolous or vexatious defence and counterclaim. It is not the function of a judge on an application such as this to say anything more about the merits of the action or the defences. That is a matter for the trial Judge.

19 The practical problem that faces the Court and the parties is that the issue of whether or not there is a debt underlying the debenture must be resolved before the receiver can be authorized to proceed with realization of the assets. The Court cannot supervise this company indefinitely through the efforts of a receiver. The action must proceed to resolution in a prompt and efficient manner. The Court will be responsive to any abuse of process or delay.

20 It is obvious that the bank will suffer a further diminution in recovery if the bank's suit proves successful. But this inequity is as a result of the contract that the bank entered into with the debtor, and the potential for unfairness and inequity or injustice occurring is less apparent than to require the debtor to go to trial of the issue between the parties without the benefit of counsel.

21 The order will go that the receiver is at liberty to pay to counsel for the debtor reasonable amounts from time to time on account of its fees incurred in connection with the defence of this action and prosecution of the counterclaim. These moneys shall come from the cash flow received by the receiver and shall only be payable after a proper reserve for the receiver's fees and out-of-pockets, and payment of the day-to-day expenses of the operation of the defendant's business have been provided. Counsel may speak to the requirement of any particular terms required to ensure there is no abuse of this procedure, and generally as counsel may advise.

Order accordingly.

End of Document

Most Negative Treatment: Distinguished
Most Recent Distinguished: Weinberg v. Loring Ward International Ltd. | 2009 MBQB 92, 2009 CarswellMan 221, 58 B.L.R. (4th) 305, 177 A.C.W.S. (3d) 408, 239 Man. R. (2d) 59 | (Man. Q.B., Apr 16, 2009)

2007 MBCA 36
Manitoba Court of Appeal

Manitoba (Securities Commission) v. Crocus Investment Fund

2007 CarswellMan 98, 2007 MBCA 36, [2007] 7 W.W.R. 32, [2007] M.J. No. 87, 156 A.C.W.S. (3d) 245, 214 Man. R. (2d) 44, 28 B.L.R. (4th) 246, 31 C.B.R. (5th) 1, 395 W.A.C. 44, 39 C.P.C. (6th) 321

The Manitoba Securities Commission (Applicant / Respondent) and Crocus Investment Fund (Respondent / Respondent) and Bernard Bellan (Intervener / Appellant) and Charles Curtis, Peter Olfert, Waldron (Wally) Fox-Decent, Lea Baturin, Albert Beal, Ron Waugh, Diane Beresford, Sylvia Farley, Robert Hilliard, Robert Ziegler, David G. Friesen, Sherman Kreiner, Jane Hawkins, James Umlah, John Clarkson and Hugh Eliasson (Interveners / Respondents)

M.A. Monnin, B.M. Hamilton, M.H. Freedman JJ.A.

Heard: November 30, 2006
Judgment: March 30, 2007
Docket: AI 06-30-06444

Proceedings: affirming *Manitoba (Securities Commission) v. Crocus Investment Fund* (2006), 2006 MBQB 19, 18 C.B.R. (5th) 143, 200 Man. R. (2d) 89, [2006] 7 W.W.R. 343, 2006 CarswellMan 33, 14 B.L.R. (4th) 229 (Man. Q.B.)

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M.G. Tadman for Intervener, R. Hilliard

Subject: Civil Practice and Procedure; Corporate and Commercial; Securities; Insolvency
Related Abridgment Classifications
Business associations
III Specific matters of corporate organization
  III.1 Directors and officers
    III.1.e Duty to manage
      III.1.e.iii Indemnification by corporation
Debtors and creditors
VII Receivers
  VII.6 Conduct and liability of receiver
    VII.6.a General conduct of receiver
Remedies
II Injunctions
  II.2 Prohibitive injunctions
    II.2.e Miscellaneous

Headnote

Remedies --- Injunctions — Rules governing injunctions — Interlocutory, interim and permanent injunctions — General principles

Test — Investigation by Auditor General into investment fund resulted in resignation of fund's board — Fund held directors' liability insurance to cap of $5,000,000 — Fund's bylaws stated that directors would be indemnified for loss if they acted in good faith and they believed conduct was lawful — Former directors and officers were presently involved in certain legal matters, including investigations by Auditor General and Manitoba Securities Commission, and proposed class action initiated by shareholders against fund — Court appointed receiver for fund — Judge authorized and directed receiver to pay all reasonably incurred ongoing legal expenses of former directors and officers, as well as amounts of any related unfavourable judgments, subject to certain rights of reimbursement — Shareholder of fund appealed — Appeal dismissed — Judge was correct in law in her decision, she acted reasonably in exercising her discretion to direct that such advances be made — Judge's analysis was not flawed because she did not apply three-part test by failing to consider question of irreparable harm — Motion about funding of legal expenses is no more than interim step during course of action which resulted in remedy solidly grounded in Corporations Act and in fund's by-law — Motion had none of extraordinary features of stay or injunction.

Debtors and creditors --- Receivers — Conduct and liability of receiver — General conduct of receiver

Investigation by Auditor General into investment fund resulted in resignation of fund's board — Fund held directors' liability insurance to cap of $5,000,000 — Fund's bylaws stated that directors would be indemnified for loss if they acted in good faith and they believed conduct was lawful — Former directors and officers were presently involved in certain legal matters, including investigations by Auditor General and Manitoba Securities Commission, and proposed class action initiated by shareholders against fund — Court appointed receiver for fund — Judge authorized and directed receiver to pay all reasonably incurred ongoing legal expenses of former directors and officers, as well as amounts of any related unfavourable judgments, subject to certain rights of reimbursement — Shareholder of fund appealed — Appeal dismissed — Judge was correct in law and acted reasonably in exercising her discretion to direct advances be made — Board of directors has wide-ranging authority to manage business and affairs of corporation pursuant to s. 97(1) of Corporations Act — Board has authority to decide that corporation should advance defence costs to persons potentially indemnified by virtue of s. 119(1) of Act, so long as board is satisfied person was made party to litigation by reason of being director or officer, costs were reasonably incurred, and person acted in good faith — Receiver acting under court direction would likewise have such authority, it being matter of judge's discretion whether and when to authorize or direct receiver to advance defence costs — Fund decided to indemnify its directors and officers, and enacted by-law to that effect pursuant to s. 119(1) of Act — There was no evidence that former directors and officers had acted other than in good faith — Under circumstances, former directors and officers ought not to be obliged to finance their own defence costs.

Business associations --- Specific corporate organization matters — Directors and officers — Duty to manage — Indemnification by corporation

Investigation by Auditor General into investment fund resulted in resignation of fund's board — Fund held directors' liability insurance to cap of $5,000,000 — Fund's bylaws stated that directors would be indemnified for loss if they acted in good faith and they believed conduct was lawful — Former directors and officers were presently involved in certain legal matters, including investigations by Auditor General and Manitoba Securities Commission, and proposed class action initiated by shareholders against fund — Court appointed receiver for fund — Judge authorized and directed receiver to pay all reasonably incurred ongoing legal expenses of former directors and officers, as well as amounts of any related unfavourable judgments, subject to certain rights of reimbursement — Shareholder of fund appealed — Appeal dismissed — Judge was correct in law and acted reasonably in exercising her discretion to direct advances be made — Board of directors has wide-ranging authority to manage business and affairs of corporation pursuant to s. 97(1) of Corporations Act — Board has authority to decide that corporation should advance defence costs to persons potentially indemnified by virtue of s. 119(1) of Act, so long as board is satisfied person was made party to litigation by reason of being director or officer, costs were reasonably incurred, and person acted in good faith — Receiver acting under court direction would likewise have such authority, it being matter of judge's discretion whether and when to authorize or direct receiver to advance defence costs — Fund decided to indemnify its directors and officers, and enacted by-law to that effect pursuant to s. 119(1) of Act — There was no evidence that former directors and officers had acted other than in good faith — Under circumstances, former directors and officers ought not to be obliged to finance their own defence costs.

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Generally — referred to

s. 95 — referred to

s. 97(1) — referred to

s. 113(2)(e) — considered

s. 117(1) — referred to

s. 119 — referred to

s. 119(1) — considered

s. 119(2) — referred to

s. 119(3) — considered

s. 119(5) — referred to

Court of Queen's Bench Act, R.S.M. 1987, c. C280

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s. 55(1) — referred to

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s. 2(1) — referred to

APPEAL by shareholder from judgment reported at *Manitoba (Securities Commission) v. Crocus Investment Fund* (2006), 2006 MBQB 19, 18 C.B.R. (5th) 143, 200 Man. R. (2d) 89, [2006] 7 W.W.R. 343, 2006 CarswellMan 33, 14 B.L.R. (4th) 229 (Man. Q.B.), authorizing and directing receiver to pay legal expenses of former directors and officers.

***M.H. Freedman J.A.*:**

Overview

1 Former directors and officers of Crocus Investment Fund (Crocus) have been, and continue to be, involved in certain legal matters. These include an investigation conducted by the Office of the Auditor General, an investigation conducted by the Manitoba Securities Commission and a proposed class action. The issue on this appeal is whether Crocus, a corporation which is not insolvent, although it is under the control of a receiver, should advance ongoing legal defence costs incurred by the former directors and officers, prior to the conclusion of the related legal matters. The judge decided that such advances should be made. The appellant in the present action, a shareholder of Crocus, has appealed the decision. In my opinion, the judge was correct in law in her decision, and she acted reasonably in exercising her discretion to direct that such advances be made.

Background

2 Apart from one new issue raised for the first time by the appellant during oral argument, which I will address below, the background to this matter is clearly set out in the judge's detailed reasons (at paras. 2-5):

> On June 28, 2005 Deloitte [& Touche Inc.] was appointed Receiver and Manager of Crocus Investment Fund. This occurrence came fast on the heels of a series of rapidly unfolding events in the months preceding. They included an investigation into the operations of Crocus by the Office of the Auditor General; an investigation into the conduct of Crocus and its officers and directors by the Manitoba Securities Commission (MSC); the issuance by the MSC of a statement of allegations which, among other things, alleged improper conduct on the part of Crocus and certain officers and directors; the release of the Provincial Auditor's report in May 2005; and the mass resignation of the Crocus Board in June 2005. The Receiver was quickly appointed by the court at the behest of the MSC to fill the void.

> Prior to June 28, 2005, Crocus had made arrangements to pay the legal counsel representing the officers and directors in the course of these investigations. ...
>
> On July 7, 2005 the Receiver received a letter from counsel for Bernard Bellan and certain other shareholders advising that they were in the process of commencing a class action lawsuit. It contained a request that the Receiver not pay any fees on behalf of any former officers and directors who might be named in the litigation. A week later, on July 12, 2005, a statement of claim was issued although to date that claim has not been certified as a class action.
>
> It is important to note that in addition to the former officers and directors named in the proposed class action other officers and directors seek reimbursement from Crocus for legal fees incurred relating to the investigation of the Auditor General and the MSC. It should also be observed that Crocus has an officers' and directors' liability insurance policy with Chubb Insurance Company of Canada to a maximum of $5,000,000.00. For ease of reference this Venture Capital Asset Protection Policy #7043-0036 is referred to as the Chubb policy.

3 Deloitte & Touche Inc., as court-appointed receiver (Receiver) of Crocus, applied for an order authorizing it to pay legal fees of former directors and officers to the date of its appointment, subject to certain rights of reimbursement. It also sought an order authorizing it to refrain from paying ongoing legal expenses of those persons until the completion of certain proceedings (or until further court order). The former directors and officers resisted that latter part of the application.

4 In comprehensive reasons the judge, *inter alia*, authorized and directed the Receiver to pay all reasonably incurred ongoing legal expenses of the former directors and officers, as well as the amounts of any related unfavourable judgments, subject to certain rights of reimbursement.

5 The appellant raised several objections to the judge's decision; his argument may be summarized this way. While as a strict matter of law the judge had the discretion to order as she did regarding the advancement of costs, she erred by (1) finding no evidence of bad faith; (2) ordering advancement of costs prior to any determination that the requirements of the governing statute had been met; (3) directing that the indemnity extend to unfavourable judgments, and (4) disregarding the absence of evidence of the ability of indemnified persons to repay any amount, if it is ultimately determined that there was no entitlement to the indemnity. Additionally, as noted, a new argument was raised at the hearing.

Statutory and Other Provisions

6 Crocus is governed by the provisions of *The Corporations Act*, C.C.S.M., c. C225 (the *Act*) (see *The Crocus Investment Fund Act*, C.C.S.M., c. C308, s. 2(1)). Like its federal counterpart, the *Canada Business Corporations Act* (*CBCA*) and other provincial corporation statutes, the *Act* contains provisions dealing with corporate indemnification of persons such as the former directors and officers. The relevant provisions of the *Act* are attached as an Appendix.

7 The main indemnification provisions are in s. 119(1) and (3). Section 119(1) states:

> **Indemnification**
>
> **119(1)** Except in respect of an action by or on behalf of the corporation or body corporate to procure a judgment in its favour, a corporation may indemnify a director or officer of the corporation, a former director or officer of the corporation or a person who acts or acted at the corporation's request as a director or officer of a body corporate of which the corporation is or was a shareholder or creditor, and his heirs and legal representatives, against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by him in respect of any civil, criminal or administrative action or proceeding to which he is made a party by reason of being or having been a director or officer of the corporation or body corporate, if
>
> (a) he acted honestly and in good faith with a view to the best interests of the corporation; and

(b) in the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, he had reasonable grounds for believing that his conduct was lawful.

8 Section 119(1) is permissive. Except in respect of an action by or on behalf of the corporation, a corporation such as Crocus may indemnify persons, such as the former directors and officers, who by virtue of their office reasonably incur legal costs in actions or proceedings, against such costs and the amount of related judgments, subject to two conditions. First, the person must have acted honestly and in good faith with a view to the corporation's best interests; this reflects part of the basic duty of a director and officer set out in s. 117(1) of the *Act*. Second, in certain instances, the person must have had reasonable grounds for believing his conduct was lawful.

9 Section 119(3) states:

Indemnity as of right

119(3) Notwithstanding anything in this section, a person referred to in subsection (1) is entitled to indemnity from the corporation in respect of all costs, charges and expenses reasonably incurred by him in connection with the defence of any civil, criminal or administrative action or proceeding to which he is made a party by reason of being or having been a director or officer of the corporation or body corporate, if the person seeking indemnity

(a) was substantially successful on the merits in his defence of the action or proceeding; and

(b) fulfils the conditions set out in clauses (1)(a) and (b).

10 Section 119(3) creates an indemnity as of right. It entitles a person such as a former director or officer to the indemnity described in the section if the two conditions in s. 119(1) are satisfied and if he or she was substantially successful in the proceeding. That is an entitlement, in those circumstances, even if the corporation has not taken any steps pursuant to s. 119(1). The entitlement is enforceable only after the proceedings are concluded.

11 Section 113(2)(e) provides that directors may be liable if they approve "a payment of an indemnity contrary to section 119."

12 The corporate by-laws of Crocus are important. By-law 1.7 (also attached as an Appendix) is the expression of a corporate intention that directors and officers shall be indemnified. This by-law is based on s. 119(1) of the *Act* and it creates a right of indemnity, again, subject to the two conditions. As well, there are indemnification provisions in severance agreements entered into by certain former officers.

The Context and the Judge's Reasons

13 This plethora of provisions relating to the subject of indemnity for costs and amounts incurred while acting in good faith suggests both a legislative and a corporate recognition of a reality which, if not entitled to judicial notice in the traditional sense, is nevertheless obvious to observers of the Canadian business scene. That reality is simply that persons who serve as directors and senior officers of corporations whose securities are widely held expect, as incidental to that service, that, when they act honestly and in good faith, they will be indemnified for costs and amounts reasonably incurred in actions or proceedings, for which they might be personally responsible. The *Act*, like its counterparts, is framed to be consistent with this reality.

14 The interplay between the policy underlying the statutory provisions and the legitimate exigencies of the corporate world was well expressed in the unanimous Supreme Court decision in *Blair v. Consolidated Enfield Corp.*, [1995] 4 S.C.R. 5 (S.C.C.). Iacobucci J., writing for the court, made the following observation which was relied on by the judge here (at para. 74):

... [T]he broad policy goals underlying indemnity provisions ... allow for reimbursement for reasonable good faith behaviour, thereby discouraging the hindsight application of perfection. Indemnification is geared to encourage responsible behaviour yet still permit enough leeway to attract strong candidates to directorships and consequently foster

> entrepreneurism. It is for this reason that indemnification should only be denied in cases of *mala fides*. A balance must be maintained. ...

15 Although the issue at present focusses on the financing of ongoing legal costs, the policy context relating to indemnification, which is inextricably linked to the reason why the costs are being incurred, is both relevant and instructive.

16 One of the cases cited by the judge in her decision was *National Bank of Canada v. Merit Energy Ltd.*, 2001 ABQB 583, [2001] 10 W.W.R. 305 (Alta. Q.B.). The position advanced there by the directors and officers of the subject bankrupt corporation was that "directors and officers require indemnities and commercial necessity dictates that these indemnities have real value" (at para. 61). The judge in *National Bank* agreed with the fundamental argument, saying: "[a]n indemnity is a well-known commercial concept business people routinely use to eliminate or reduce risk and should be recognized as a necessary and desirable obligation" (at para. 67).

17 The judge referred also to *Canada Deposit Insurance Corp. v. Canadian Commercial Bank* (1989), 61 D.L.R. (4th) 161 (Alta. C.A.). In that case, the equivalent provision of s. 119(1) was not the governing section, because the action was one on behalf of the corporation itself, thus bringing into play the exception in the opening words: "[e]xcept in respect of an action by or on behalf of the corporation." The Alberta Court of Appeal held that, under the equivalent of s. 119(2) and (3), the right to an indemnity depended on the result of the action, so prior to the conclusion of the lawsuit ongoing defence costs could not be advanced.

18 The other case noted by the judge was *Chromex Nickel Mines Ltd. v. British Columbia (Securities Commission)* (1991), 4 B.L.R. (2d) 189 (B.C. S.C.). The British Columbia Securities Commission was investigating the president of Chromex. The board passed a resolution to indemnify him. Chromex and the president then sought a declaration that the indemnification was authorized under s. 124(1) of the *CBCA*, the equivalent of s. 119(1) of the *Act*. The Commission argued that indemnification had to wait until the proceedings were over and until the president was substantially successful. This argument failed.

19 Errico J. of the British Columbia Supreme Court found that the *CBCA* authorized Chromex to indemnify the president against legal expenses actually incurred. In the course of his reasons, he said (at paras. 8, 11-13):

> ... Section 124(3) is directed to circumstances where the applicant has the right to indemnity and s. 124(1) to circumstances where the corporation is permitted to indemnify. ...
>
> I do not think that the decision in *Canada Deposit Insurance Corp.*, supra, is authority for the proposition that ... s. 124(1) requires that the action be concluded before indemnity may be given.
>
> ... [N]o [court] approval is required under s. 124(1) and it is for the corporation through its directors, to determine if the applicant for indemnification has satisfied the conditions. ...
>
> I am reinforced in my conclusions by consideration of s. 118(2) of the Act which reads:
>
> > (2) Directors of a corporation who vote for or consent to a resolution authorizing
> >
> > . . . . .
> >
> > (e) a payment of an indemnity contrary to section 124,
> >
> > . . . . .
> >
> > are jointly and severally liable to restore to the corporation any amounts so distributed or paid and not otherwise recovered by the corporation.
>
> That section provides that the directors of a corporation are personally liable to ensure that the conditions set out in subss. 124(1)(a) and (b) are met. This does not suggest that they must await the outcome of the proceeding to grant indemnity, although it might be prudent for them to do so. Rather, it places the responsibility for compliance with s. 124 on those directors.

20 The judge said (at para. 33), and I agree with her, that *Chromex* stands for two propositions: that there is no statutory requirement to pay ongoing defence costs, and that if a corporation decides to pay such costs, payment need not await the completion of proceedings.

21 The judge concluded that there is a discretion in the court to direct payment of ongoing defence costs, or to delay such payment until substantial completion of the proceedings. She also found that the former directors and officers had a legitimate need for legal representation, and that there was no evidence of dishonesty or bad faith on their part. She found *Blair* to be persuasive, and said that it favoured payment of reasonable defence costs on an ongoing basis. She said (at paras. 45-46):

> Whereas it is recognized that the court should always exercise prudence in circumstances such as these, and particularly where the protection of s. 113 of **The Corporations Act** is not available, I am satisfied that those who are entitled to potential indemnification should be presumed to have acted in good faith in the absence of evidence to the contrary and should receive payment on an ongoing basis of all reasonable defence costs incurred. ...
>
> As agreed, I make no finding as to the entitlement of any individual former officer or director. It will be up to the Receiver, or alternatively the court, to make that determination on proper evidence. Should it happen that defence costs are paid and conduct which would disqualify a former officer and director subsequently comes to light, such payments would necessarily cease and the Receiver would be entitled to make a claim for reimbursement with interest at the Receiver's earned rate.

22 The judge's order authorized and directed that the Receiver pay:

> ... [A]ll reasonably incurred past and future legal expenses of former officers and directors on an on-going basis, and any resulting unfavourable judgments arising from the investigation of the Office of the Auditor General, proceedings taken by the Manitoba Securities Commission, the proposed class action proceeding ...

unless those persons did not meet the applicable qualifying criteria in s. 119(1) (or the related Crocus by-law or individual indemnity agreements). The order also required undertakings to repay funds if it is ultimately determined that the individual was not entitled to the indemnity.

Analysis

(1) New Argument on Appeal

23 I noted earlier that the appellant raised an argument at the hearing that had not been identified in his notice of appeal or factum. He argued that the motion by the Receiver, being an interim or interlocutory motion, should have been decided in accordance with the three-part test set out in *Metropolitan Stores (MTS) Ltd. v. Manitoba Food & Commercial Workers, Local 832*, [1987] 1 S.C.R. 110 (S.C.C.), and affirmed in *RJR-MacDonald Inc. v. Canada (Attorney General)*, [1994] 1 S.C.R. 311 (S.C.C.). In particular, he argued, the judge did not consider the question of irreparable harm, an integral part of the test. He was not able to point to any authority for his argument that the three-part test should apply in a circumstance like this.

24 The three-part test applies in cases of interlocutory injunctions and stays of proceedings. It would also apply in other circumstances where a remedy is sought which, if granted, would impact the respondent as profoundly and potentially permanently as does a stay or an injunction. See Beetz J. in *Metropolitan Stores* (at p. 127):

> A stay of proceedings and an interlocutory injunction are remedies of the same nature. In the absence of a different test prescribed by statute, they have sufficient characteristics in common to be governed by the same rules and the courts have rightly tended to apply to the granting of interlocutory stay the principles which they follow with respect to interlocutory injunctions... .
>
> [Emphasis added]

25 Both interlocutory injunctions and stays are recognized, for good reason, as "extraordinary" remedies (see, e.g., *Bhattacharya v. St. Boniface General Hospital*, 2000 MBCA 51, 148 Man. R. (2d) 115 (Man. C.A.), and *Merck & Co. v. Apotex Inc.*, 2003 FCA 234, 227 D.L.R. (4th) 106 (Fed. C.A.)). Nothing about this case meets that description. This motion about the funding of legal expenses is no more than an interim step during the course of an action which resulted in a remedy solidly grounded in the *Act* and in Crocus's by-law. It has none of the extraordinary features of a stay or an injunction.

26 In *Metropolitan Stores*, Beetz J. referred to tests prescribed by statute. It is clear that different tests have been legislated when a party seeks an interlocutory injunction, and when a receiver seeks relief from a court. In the first instance, *The Court of Queen's Bench Act*, C.C.S.M., c. C280, gives the court power to grant an injunction when it is "just or convenient to do so" (s. 55(1)). The three-part test applies on such an application; see, e.g., *T-W Insurance Brokers Inc. v. Manitoba Public Insurance Corp.* (1997), 115 Man. R. (2d) 305 (Man. C.A.), and *4849052 Manitoba Ltd. v. Cairns*, 2005 MBQB 9, 207 Man. R. (2d) 7 (Man. Q.B.).

27 On the other hand, this application by the Receiver is governed by the *Act* (s. 95) which gives the court authority on such an application to "make any order it thinks fit." (See also, s. 119(5).) There is a conceptual distinction between the two standards. See *Ross v. Ross* (1984), 39 R.F.L. (2d) 51 (Man. C.A.), where Matas J.A. said (at p. 63):

> One of the meanings listed in The Oxford Universal Dictionary for "fit" is "Suited to the circumstances of the case, answering the purpose, proper or appropriate". As for "just", one of its definitions reads: "Consonant with the principles of moral right; equitable; fair. Of rewards, punishments, etc.: Merited. Constituted by law or by equity, lawful, rightful; legally valid." ...

28 There are different words used in the two statutes, and different tests are applicable. The standard is different when a court deals with a motion relating to indemnities and legal fees, which in my view does not lead to an extraordinary remedy, and when a court grants an interim injunction or a stay.

29 Even in certain cases of stays courts have sometimes not applied the three-part test. This may occur where the request is for an interlocutory stay of proceedings before a court, unlike the situation in *Metropolitan Stores* where the proceedings were before an administrative tribunal. A number of cases of stays of court proceedings have applied the test of whether the interests of justice clearly outweigh the respondents' right to proceed with their cause of action. See, *Assn. of Parents Support Groups Ontario Inc. v. York* (1987), 14 C.P.R. (3d) 263 (Fed. T.D.), and *Alberta v. Canada (Minister of Environment)* (1991), 46 F.T.R. 40 (Fed. T.D.).

30 All the authority I can find supports the view that the judge's analysis was not flawed because she did not apply the three-part test. I conclude that there is no merit in this argument.

(2) Corporate Indemnification and Advancement of Defence Costs

31 Pursuant to s. 119(1) of the *Act*, a corporation governed by the *Act*, like Crocus, may decide to indemnify its directors and officers. Crocus has so decided, and enacted By-law 1.7 pursuant to that section. Indemnification under that section (in contrast to the s. 119(3) indemnification) is permissive, but once a corporation decides to act under that section the indemnity becomes an entitlement subject only to the satisfaction of conditions (a) and (b). The right to be indemnified may, but will not necessarily, later be negated by the outcome of the lawsuit, that is, if it transpires that conditions (a) or (b) were not satisfied.

32 The policy underlying the indemnification provisions was explained in *Blair*. As the judge noted, *Blair*, like the other cases cited by her, is factually distinguishable from the present situation. Nevertheless, it provides clear guidance to the proper interpretation of the statutory provisions.

33 *Blair* involved a battle for control of a corporation. Mr. Blair was the corporation's president and chaired a shareholders' meeting. In doing so, he acted on legal advice. He sought indemnification for his legal costs. The issue was not advancement of

costs, but rather, as Iacobucci J. said for a unanimous court: "who should bear the costs of legally contesting a disputed directors' election: the corporation, or the chairman in his personal capacity...?" (at para. 2).

34 Whether Mr. Blair had acted in good faith was an issue. Iacobucci J. stated, as a premise, that (at para. 35):

> ... [P]ersons are assumed to act in good faith unless proven otherwise: *General Motors of Canada Ltd. v. Brunet*, [1977] 2 S.C.R. 537, at p. 548. In this respect, contrary to the appellant's submissions before this Court, I believe that a proper construction of the statute and law related to good faith issues reveals that Blair is not required to prove his good faith, although he may certainly call evidence in this regard to counter whatever evidence of bad faith may be adduced against him. To a large extent, it is the corporation that must establish, to the satisfaction of the court, exactly what Blair did that was inimical to its best interests.

35 In the present case there was no evidence before the judge that could support any finding that the former directors and officers had acted other than in good faith. This is an important point, to which I will return.

36 Iacobucci J. then identified the three conditions that must exist "in order to receive indemnification for the costs of defending in litigation" (at para. 36):

> (1) the person must have been made a party to the litigation by reason of being a director or an officer of the corporation;
>
> (2) the costs must have been reasonably incurred; and
>
> (3) the person must have acted honestly and in good faith with a view to promoting the best interests of the corporation.

37 The court found that Mr. Blair had met all three conditions. Moreover, permitting Mr. Blair to be indemnified conformed to "the broad policy goals underlying indemnity provisions" (at para. 74), and see para. 14 above).

38 Iacobucci J. also said (at para. 75):

> Given the circumstances of this appeal, denying Blair indemnification would, in my mind, run afoul of these policy concerns. See also Daniels and Hutton, "The Capricious Cushion: The Implications of the Directors' and Officers' Insurance Liability Crisis on Canadian Corporate Governance" (1993), 22 *Can. Bus. L.J.* 182, at p. 187:
>
> > To temper excessive care and activity level reactions to potential gatekeeper liability, modern corporate law statutes permit a corporation to indemnify a director for any expense reasonably incurred in defending, settling or satisfying a judgment for any action, provided that the director's fiduciary duty to act "honestly and in good faith and with a view to the best interests of the corporation" has been fulfilled.

39 Mainly on the persuasive reasoning articulated in *Blair*, the judge found that the circumstances favoured advancement of defence costs on an ongoing basis for the benefit of the former directors and officers. There was no evidence before her of dishonesty or bad faith, and she said that good faith must, therefore, be presumed (at para. 44-45).

40 The appellant referred to "serious allegations of wrongdoing" and argued that the Auditor General's report, the allegations of the Manitoba Securities Commission, and the existence of the receivership all point to a misleading of shareholders by the former directors and officers which constitute evidence of bad faith. That is not correct. There was no evidence of bad faith before the judge, even taking into account that "the concept of bad faith can and must be given a broader meaning that encompasses serious carelessness or recklessness" (*McCullock Finney c. Barreau (Québec)*, 2004 SCC 36, [2004] 2 S.C.R. 17 (S.C.C.) at para. 39). Allegations in pleadings or by the Manitoba Securities Commission, or the extra-judicial conclusions of the Auditor General, are not evidence, and cannot, unless and until they are established in a legal proceeding, displace the presumption of good faith which is well recognized at law.

41 The essence of the judge's decision is set out in two conclusions. First: "I am satisfied that those who are entitled to potential indemnification should be presumed to have acted in good faith in the absence of evidence to the contrary" (at para. 45). There is ample authority in *Blair* for this conclusion.

42 Second, she continued: "... and [they] should receive payment on an ongoing basis of all reasonable defence costs incurred" (*ibid.*).

43 The *Act*, and its federal counterpart, the *CBCA*, were each enacted, and then amended, in the 1970's. It was recognized at some later point that the statutory provisions were not as clear as they might be on the present question, the advancement of legal costs under the indemnity provisions (see Lyne Tassé, *Canada Business Corporations Act, Discussion Paper, Director's Liability* (Ottawa: Industry Canada, 1995). In 2001 the *CBCA* was amended such that s. 124(2) now reads:

> **Advance of costs**
>
> **(2)** A corporation may advance moneys to a director, officer or other individual for the costs, charges and expenses of a proceeding referred to in subsection (1). The individual shall repay the moneys if the individual does not fulfil the conditions of subsection (3).

44 No similar amendment has been made to the *Act*. Nevertheless, while such an amendment would remove any doubt about a corporation's authority to advance costs, I am satisfied that even without that amendment, a corporation governed by the *Act* has the power to make such advances in appropriate cases.

45 The appellant acknowledges that a corporation has broad powers of indemnification and advancement of costs. His factum states: "the board of directors of a corporation may vote to authorize indemnification of officers and directors for defence costs prior to the conclusion of litigation pursuant to s. 119(1)."

46 The appellant further recognizes that a judge has broad discretion when considering a receiver's application, such as the one before her: "[i]n a receivership, the court has discretion to determine *when* and whether directors' legal costs should be indemnified" (emphasis added).

47 The board of directors of a corporation has wide-ranging authority to manage the business and affairs of the corporation (see s. 97(1) of the *Act*). In my opinion it is within the power and authority of a board to decide that the corporation should advance defence costs to persons potentially indemnified by virtue of s. 119(1), so long as the board is satisfied that the three conditions referred to above (see para. 36) are satisfied. It would normally be expected that a board would require the kind of repayment undertaking that was required and obtained here.

48 Since a board of directors would have the authority described above, so would a receiver acting under court direction. It is, then, as the appellant accepts, a matter of a judge's discretion whether and when to authorize or direct the receiver to advance defence costs.

49 The appellant argued that in exercising her discretion, the judge erred in finding no evidence of bad faith, an argument I dealt with earlier. He also argued error in that there has been no judicial determination that the conditions in s. 119(1) have been satisfied, but that is a flawed argument. With the presumption of good faith, absent evidence to the contrary, the conditions in s. 119(1) must be presumed to be satisfied until it is established otherwise. To adopt the appellant's argument would be to convert the s. 119(1)/By-law 1.7 entitlement into a s. 119(3) entitlement, which delays enforcement until proceedings are over. That is not what is meant by the indemnity provisions in the *Act*.

50 The judge's decision is founded on sound legal principles and is consistent with the commercial exigencies spoken of in *National Bank* and *Blair*. While it is possible that the present lawsuit will be resolved in short order, it is more likely that it will take some time before that happens. I agree with the judge when she said: "[t]hese matters are lengthy and complex and are unlikely to be completed for some considerable time" (at para. 41). In the meantime, the former directors and officers, presumed

so far to have acted in good faith, have an immediate and legitimate need for counsel. Under the present circumstances they ought not to be obliged to finance their own defence costs.

51 The judge had the discretion to order the advancement. Consistent with the policy rationale explained in *Blair*, she had a sound basis for exercising her discretion as she did. In doing so, she directed that undertakings from the former directors and officers be obtained, promising repayment if it subsequently developed that "he or she was not entitled to payment," thus ensuring so far as possible that the interests of other stakeholders were protected.

52 Viewed from the corporation's perspective, a decision to advance defence costs is an interim financing decision. Based on the criteria and safeguards applicable here, the corporation is not necessarily at risk. I agree with the following observations of Chancellor Allen of the Delaware Court of Chancery in *Advanced Mining Systems Inc. v. Fricke*, 623 A.2d 82 (U.S. Del. Ch. 1992) which, while in the context of statutory language closer to the present *CBCA* than the *Act*, is nevertheless applicable (at p. 84):

> ... [T]he decision to extend advancement rights should ultimately give rise to no net liability on the corporation's part. The corporation maintains the right to be repaid all sums advanced, if the individual is ultimately shown not to be entitled to indemnification. Thus the advancement decision is essentially simply a decision to advance credit.

53 And that is the situation here. If a former director or officer ultimately is entitled to indemnification, costs would be part of that entitlement. If a former director and officer is ultimately disentitled to indemnification, that person has undertaken to pay back all advanced costs.

54 The appellant argued before us that the judge ought to have considered the ability of indemnified persons to repay amounts, if required to do so. While the obligation to repay is clear, the ability to do so in each case has not been assessed. The judge did not require security for the repayment undertakings. It was within her discretion, as it would have been in the discretion of Crocus's board of directors, not to require such security. The implications of a decision to require security might be significant, but no such decision was made here, so consideration of those implications will be left for another day.

55 The reasons of the judge, and the related parts of her order, authorizing the Receiver to pay judgments unless the former directors and officers are not entitled to be indemnified, do no more than express in judicial form what is already permitted by s. 119(1) and mandated by Crocus's By-law. While the appellant objected to this part of the order, there is no justifiable basis for the objection.

Conclusion

56 As a general principle, we should be "highly reluctant" to interfere with the exercise of the judge's discretion (*Elsom v. Elsom*, [1989] 1 S.C.R. 1367 (S.C.C.), at 1374). There was no misdirection by the judge, nor any wrong amounting to an injustice (see *Elsom*, at p. 1374). Her decision was correct in law and the exercise of her discretion was reasonable. The decision should be endorsed, and I would dismiss the appeal with costs.

Appeal dismissed.

APPENDIX

The Corporations Act

Duty to manage or supervise management

97(1) Subject to any unanimous shareholder agreement, the directors shall manage, or supervise the management of, the business and affairs of a corporation.

Further liability of directors

113(2) Directors of a corporation who vote for or consent to a resolution authorizing

. . . . .

(e) a payment of an indemnity contrary to section 119;

are jointly and severally liable to restore to the corporation any amounts so distributed or paid and not otherwise recovered by the corporation.

Duty of care of directors and officers

117(1) Every director and officer of a corporation in exercising his powers and discharging his 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.

Indemnification

119(1) Except in respect of an action by or on behalf of the corporation or body corporate to procure a judgment in its favour, a corporation may indemnify a director or officer of the corporation, a former director or officer of the corporation or a person who acts or acted at the corporation's request as a director or officer of a body corporate of which the corporation is or was a shareholder or creditor, and his heirs and legal representatives, against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by him in respect of any civil, criminal or administrative action or proceeding to which he is made a party by reason of being or having been a director or officer of the corporation or body corporate, if

(a) he acted honestly and in good faith with a view to the best interests of the corporation; and

(b) in the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, he had reasonable grounds for believing that his conduct was lawful.

Indemnification in derivative actions

119(2) A corporation may with the approval of a court indemnify a person referred to in subsection (1) in respect of an action by or on behalf of the corporation or body corporate to procure a judgment in its favour, to which he is made a party by reason of being or having been a director or an officer of the corporation or body corporate, against all costs, charges and expenses reasonably incurred by him in connection with the action if he fulfils the conditions set out in clauses (1)(a) and (b).

Indemnity as of right

119(3) Notwithstanding anything in this section, a person referred to in subsection (1) is entitled to indemnity from the corporation in respect of all costs, charges and expenses reasonably incurred by him in connection with the defence of any civil, criminal or administrative action or proceeding to which he is made a party by reason of being or having been a director or officer of the corporation or body corporate, if the person seeking indemnity

(a) was substantially successful on the merits in his defence of the action or proceeding; and

(b) fulfils the conditions set out in clauses (1)(a) and (b).

Directors' and officers' insurance

119(4) A corporation may purchase and maintain insurance for the benefit of any person referred to in subsection (1) against any liability incurred by him

(a) in his capacity as a director or officer of the corporation, except where the liability relates to his failure to act honestly and in good faith with a view to the best interests of the corporation; or

(b) in his capacity as a director or officer of another body corporate where he acts or acted in that capacity at the corporation's request, except where the liability relates to his failure to act honestly and in good faith with a view to the best interests of the body corporate.

Application to court

119(5) A corporation or a person referred to in subsection (1) may apply to a court for an order approving an indemnity under this section and the court may so order and make any further order it thinks fit.

Notice to director

119(6) An applicant under subsection (5) shall give the Director notice of the application, and the Director is entitled to appear and be heard in person or by counsel.

Other notice

119(7) Upon an application under subsection (5), the court may order notice to be given to any interested person and that person is entitled to appear and be heard in person or by counsel.

Crocus By-Law

1.7 Indemnity of Officers and Directors: Each Officer and each Director of the Fund and each former Officer and each former Director of the Fund and each person who acts and/or has acted at the Fund's request as a Director or Officer of a body corporate of which the Fund is or was a Shareholder or creditor and her or his heirs and legal representatives shall be indemnified against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by her or him in respect of any civil, criminal or administrative action or proceeding to which she or he is made a party by reason of being or having been a Director or Officer of the Fund, if

(a) she or he acted honestly and in good faith with a view to the best interests of the Fund; and

(b) in the case of criminal or administrative action or proceeding that is enforced by a monetary penalty, she or he had reasonable grounds for believing that her or his conduct was lawful.

Most Negative Treatment: Distinguished
Most Recent Distinguished: Boily v. Carleton Condominium Corp. 145 | 2014 ONCA 574, 2014 CarswellOnt 10591, 116 W.C.B. (2d) 26, 322 O.A.C. 261, [2014] O.J. No. 3625, 242 A.C.W.S. (3d) 555, 376 D.L.R. (4th) 60, 121 O.R. (3d) 670 | (Ont. C.A., Aug 6, 2014)

2009 ONCA 198
Ontario Court of Appeal

Bennett v. Bennett Environmental Inc.

2009 CarswellOnt 1132, 2009 ONCA 198, [2009] O.J. No. 853, 175 A.C.W.S. (3d) 421, 264 O.A.C. 198, 308 D.L.R. (4th) 530, 53 B.L.R. (4th) 100, 94 O.R. (3d) 481

John Anthony Bennett (Applicant / Respondent) and Bennett Environmental Inc. (Respondent / Appellant)

S.E. Lang, R.G. Juriansz, G. Epstein JJ.A.

Heard: November 25, 2008
Judgment: March 5, 2009
Docket: CA C48644

Proceedings: affirming *Bennett v. Bennett Environmental Inc.* (2008), 2008 CarswellOnt 7285 (Ont. S.C.J.)

Counsel: Linda M. Plumpton, Andrew D. Gray for Appellant
Nigel Campbell, Bruce O'Toole for Respondent

Subject: Corporate and Commercial; Securities
Related Abridgment Classifications
Business associations
III Specific matters of corporate organization
III.1 Directors and officers
III.1.e Duty to manage
III.1.e.iii Indemnification by corporation
Business associations
III Specific matters of corporate organization
III.1 Directors and officers
III.1.i Miscellaneous
Headnote
Business associations --- Specific corporate organization matters — Directors and officers — Miscellaneous issues
Indemnification — Company remediated contaminated soil — B was company's CEO and was later chair of company's board of directors — In June 2003, company announced that it was awarded largest soil remediation contract in its history — Company was told that competitor was protesting award of contract and was informed in August and September 2003 that contract was going to be re-bidded — Company won contract again but for smaller amount of soil — Company continued to list prior contract in inventory of projects — In June 2004, company disclosed that it had been awarded smaller contract and that status of contract had been in dispute since August 2003 — Company's share price fell almost 50 per cent within ten days — Company, B and other directors were subject to class action and securities proceedings in United States and Ontario — B sought indemnification from company — Company refused — B brought application for declaration that he was entitled to indemnification for all proceedings — Application judge held that company failed to establish that B did not satisfy requirements of s. 124(3) of Canada Business Corporations Act and company was ordered to indemnify B — Company appealed — Appeal dismissed — Issue

arose as to interpretation of s. 124(3)(b) — Company should bear burden of establishing that director did not have reasonable grounds for his or her belief that conduct was lawful — Consideration must be given as to whether director acted reasonably when director's conduct or belief was considered in context of perspective of director in comparable circumstances at time — Examination of comparable circumstances required analysis of issue from perspective of knowledge and skill set of director and information and advice upon which director's conduct or belief was based.

Business associations --- Specific corporate organization matters — Directors and officers — Duty to manage — Indemnification by corporation

Company remediated contaminated soil — B was company's CEO and was later chair of company's board of directors — In June 2003, company announced that it was awarded largest soil remediation contract in its history — Company was told that competitor was protesting award of contract and was informed in August and September 2003 that contract was going to be re-bidded — Company won contract again but for smaller amount of soil — Company continued to list prior contract in inventory of projects — In June 2004, company disclosed that it had been awarded smaller contract and that status of contract had been in dispute since August 2003 — Company's share price fell almost 50 per cent within ten days — Company, B and other directors were subject to class action and securities proceedings in United States and Ontario — B sought indemnification from company — Company refused — B brought application for declaration that he was entitled to indemnification for all proceedings — Application judge held that company failed to establish that B did not satisfy requirements of s. 124(3) of Canada Business Corporations Act and company was ordered to indemnify B — Company appealed — Appeal dismissed — B acknowledged that contract dispute was material change that company was obliged to disclose — B gave reasons why he did not take information about change in contract seriously — Honesty of B's belief was supported by absence of motive to withhold disclosure — Company failed to establish that B's stated belief was either opportunistic or amounted to reckless disregard of his obligations — Company failed to demonstrate that from perspective of someone in B's position at time, B did not have reasonable grounds to believe that he was acting lawfully — It was open to application judge to determine that company did not establish that B did not have reasonable grounds to believe his conduct was lawful.

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Catalyst Fund General Partner I Inc. v. Hollinger Inc. (2006), 2006 CarswellOnt 1416, 15 B.L.R. (4th) 171, 208 O.A.C. 55, 79 O.R. (3d) 288, 266 D.L.R. (4th) 228 (Ont. C.A.) — considered

Entreprises Sibeca inc. c. Frelighsburg (Municipalité) (2004), *(*sub nom. *Entreprises Sibeca Inc. v. Frelighsburg (Municipality))* 243 D.L.R. (4th) 513, 2004 SCC 61, 2004 CarswellQue 2404, 2004 CarswellQue 2405, [2004] 3 S.C.R. 304, 4 M.P.L.R. (4th) 1, *(*sub nom. *Entreprises Sibeca Inc. v. Frelighsburg (Municipalité))* 325 N.R. 345, 27 R.P.R. (4th) 1 (S.C.C.) — considered

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s. 136 — referred to
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s. 119 — referred to
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s. 124 — referred to

s. 124(1) — referred to

s. 124(3) — considered

s. 124(3)(a) — considered

s. 124(3)(b) — considered
Companies Act, R.S.N.S. 1989, c. 81
s. 204 — referred to

s. 205 — referred to
Companies Act, R.S.P.E.I. 1988, c. C-14
s. 64 — referred to
Corporations Act, R.S.M. 1987, c. C225
s. 119 — referred to
Corporations Act, R.S.N. 1990, c. C-36
s. 90 — referred to

s. 184 — referred to
Securities Act, R.S.O. 1990, c. S.5
Generally — referred to

s. 75 — referred to

s. 122(1)(b) — referred to

s. 122(3) — referred to

APPEAL by company from judgment reported at *Bennett v. Bennett Environmental Inc.* (2008), 2008 CarswellOnt 7285, 53 B.L.R. (4th) 89 (Ont. S.C.J.), requiring company to indemnify director.

***S.E. Lang J.A.*:**

1 This appeal concerns the interpretation and application of a statutory provision that, in certain circumstances, prohibits corporations from indemnifying officers and directors for the financial consequences of their regulatory offences. It arises in an appeal by Bennett Environmental Inc. (BEI) from a March 4, 2008 order. In that order, notwithstanding s. 124(3) of the *Canada Business Corporations Act*, R.S.C. 1985, c. C-44 (the CBCA), the application judge required BEI to indemnify its

former corporate director, John Anthony Bennett, for all costs, charges and expenses arising from certain civil and administrative proceedings, including proceedings under the *Securities Act*, R.S.O. 1990, c. S.5.

Background

2 BEI, a company publicly traded on both the Toronto and American Stock Exchanges, is a federally incorporated company. It carries on a business that includes the thermal remediation of contaminated soil. Bennett, the founder of BEI's predecessor company, was BEI's Chief Executive Officer and a member of its two-person Disclosure Committee. After Bennett resigned from both positions in February 2004, he was no longer involved in the details of management. However, he served as chair of BEI's Board of Directors until August 2004 and thereafter continued as a consultant to BEI.

3 In June 2003, BEI announced it had been awarded the largest soil remediation contract in its history, called the Phase III Contract (the Contract). The Contract was executed with Sevenson Environmental Services Inc. (Sevenson), which acted as subcontractor for the United States Army Corps of Engineers (the Corps). BEI had previously entered into and fulfilled similar contracts in the first two phases of the same soil remediation project.

4 After its announcement, BEI was notified in June 2003 that a competitor was protesting the award of the Contract to BEI. In August and September, 2003, BEI was notified that the Corps asserted a withdrawal of its consent to the award of the Contract to BEI and that the Corps was rebidding a contract (the Second Contract) through Sevenson for a much smaller volume of soil. Nonetheless, in intervening press releases, BEI continued to list the Contract, including its large volume of soil remediation, as part of its inventory of projects. In June 2004, BEI executed the Second Contract. That month and the next, the Corps definitively took the position that the Contract was at an end and that the Second Contract was the only outstanding contract.

5 In July 2004, BEI issued a press release disclosing that further shipments under the Contract were "highly unlikely" and that it had been awarded the smaller Second Contract. In the same press release, BEI disclosed that the status of the Contract had been in dispute since August 2003. The price of BEI shares fell almost 50% within ten days.

6 After the dramatic loss in share value, class actions were brought in the United States against BEI and BEI directors. As well, the U.S. Securities and Exchange Commission (the SEC) brought proceedings against BEI, Bennett, and other BEI directors. The class actions and SEC proceedings were ultimately settled in 2005 and 2006.

The Ontario Securities Commission Proceedings

7 In addition to the proceedings brought in the U.S., the staff of the Ontario Securities Commission (the OSC) also made allegations against BEI, Bennett, and other BEI directors, which included alleged violations of the disclosure requirements under the *Securities Act*. The OSC later abandoned an allegation that Bennett had provided misleading evidence during its investigation. There was no allegation of insider trading against Bennett, although his successor at BEI admitted to that offence.

8 In 2006, the OSC approved a settlement agreement between its staff and Bennett. In that agreement, Bennett admitted that, at the time it arose, the existence of the dispute about the Contract constituted a "material change" within the meaning of the *Securities Act* and that BEI had failed to disclose that change, contrary to s. 75 of the *Securities Act* and the public interest. In view of that admission, Bennett acknowledged "serious misconduct" in the violation of s. 122(1)(b) and s. 122(3) of the *Securities Act.* At the same time, the settlement agreement expressly acknowledged that Bennett had had an honest but mistaken belief that, despite the dispute, the Contract was enforceable and the dispute would ultimately be resolved in favour of BEI.

9 In accordance with the terms of the settlement agreement, the OSC prohibited Bennett from acting as an officer or director for a period of ten years, issued a reprimand, and ordered him to pay an administrative fine of $250,000, as well as $50,000 toward the cost of the OSC investigation. BEI was not ordered to pay any penalty.

The Indemnification Proceedings

10 In December 2006, Bennett sought indemnification from BEI for both the fine and the costs he had incurred in the OSC proceedings. However, BEI not only refused Bennett's request for OSC-related indemnification, but it also sought repayment of

monies it had already advanced to indemnify Bennett in relation to the U.S. class action and the costs of the SEC proceedings. The minutes of BEI's Board meeting reflect this decision and refer to the prohibition against indemnification contained in its by-law as well as "limited cash resources" from which to indemnify Bennett. In response, Bennett brought an application for a declaration that he was entitled to indemnification in relation to all the proceedings.

11 Section 124(1) of the CBCA permits indemnification of a director or officer by the corporation for all costs, charges, or expenses incurred "in respect of any civil, criminal, administrative, investigative or other proceeding in which the individual is involved because of that association with the corporation". BEI's General By-law No. 1, on the other hand, mandates indemnification.

12 However, s. 124(3) of the CBCA and BEI's by-law, which echoes the wording of s. 124(3), prohibit indemnification where the director or officer has not complied with certain requirements. The non-indemnification provisions of ss. 124(3)(a) and (b) of the CBCA contain two components, which are sometimes referred to as the "good faith and lawful conduct requirements":

> *A corporation may not indemnify an individual* under subsection (1) *unless the individual*
>
> (a) *acted honestly and in good faith with a view to the best interests of the corporation*, or, as the case may be, to the best interests of the other entity for which the individual acted as director or officer or in a similar capacity at the corporation's request; *and*
>
> (b) *in the case of a* criminal or *administrative action or proceeding that is enforced by a monetary penalty, the individual had reasonable grounds for believing that the individual's conduct was lawful.* [Emphasis added.]

13 In his affidavits in support of his application for indemnification, and in his cross-examination on those affidavits, Bennett attested that he did not consider the Contract to be in jeopardy. He also attested that he did not take seriously the Corps' notification in the summer and fall of 2003 that it was withdrawing its consent to the Contract. In Bennett's view, the Corps was only stating this position to placate the competitor who had protested the award of the Contract to BEI.

14 Bennett held this view because he considered such protests were standard and to be expected in the industry. Bennett was certain that the Contract remained extant because, from his extensive experience in the industry, he knew that BEI was the only company that could fulfill the Contract, BEI had been the successful bidder for Phases I and II of the project, and both BEI's U.S. representative and Sevenson's representative had assured BEI and Bennett that the Contract remained binding. Even when the Corps spoke of tendering a Second Contract, which Bennett believed would be for soil additional to the outstanding Contract, Bennett believed that this again was only done to placate the competitor. BEI and Bennett turned out to be wrong.

15 As evidence of the sincerity of his belief at the time in the binding nature of the Contract, Bennett pointed out that he had received his October 2003 bonus in the form of stock options instead of cash. In addition, against the advice of his financial adviser, he had refused to sell any BEI stock during the relevant period. This conduct, he argued, belied any director misconduct on his part.

16 BEI, on the other hand, asserted that Bennett had not held his belief honestly and, even if he had, that such a belief was unreasonable. Moreover, BEI took the position that Bennett could not have acted in good faith, or have had reasonable grounds for his belief, when he did not consult with legal counsel. Accordingly, BEI argued that it was prohibited by both its by-law and s. 124(3) of the CBCA from indemnifying Bennett.

The Application Judge's Reasons

17 The application judge noted Bennett's position and BEI's argument that Bennett had not fulfilled either requirement of s. 124(3). He also recognized BEI's view that a person in Bennett's position, who considered all the available information, would or should have known that BEI was required to disclose the Contract dispute, and that Bennett's position to the contrary was "untenable".

18 The application judge described the proceeding as raising the issue of whether the director seeking indemnification or the company opposing indemnification bears the onus of establishing the presence or absence of the director's "honesty, good faith and belief in lawful conduct". He quoted both prongs of the s. 124(3) requirement for indemnification. He determined that the onus fell on BEI to demonstrate that Bennett did not satisfy the requirements of s. 124(3) and that the correct test is reflected by asking the following question: "what would have been done by a reasonable person in the circumstances by a person acting as a director who possessed the skill, training and experience of the individual in question?" The application judge also recognized that a reasonable director is "not entitled to rely on an unreasonable subjective belief."

19 Since BEI had failed to establish that Bennett had acted "in bad faith or unlawfully", or that his belief in the lawfulness of his conduct was "unfounded or totally unreasonable", and since there was "no conclusive objective evidence" on which "to conclude that Bennett should not be believed on his version of the events", the application judge ordered BEI to indemnify Bennett.

Issues

20 BEI challenges both the application judge's interpretation and application of the appropriate tests required by s. 124(3) as well as his factual findings. BEI also argues that indemnification in the circumstances of this case is inconsistent with the policy rationale underlying s. 124.

21 For the reasons that follow, I would dismiss the appeal.

Analysis

Standard of review

22 Counsel agree that questions of law are to be reviewed on the standard of correctness, questions of fact and factual inference on the standard of palpable and overriding error, and questions of mixed fact and law, generally speaking, on a spectrum between the other two standards, dependent on whether the alleged error is closer to an error of law or one of fact.

The Policy Rationale

23 In interpreting the relevant provisions, I begin with the legislative rationale for permitting indemnification generally, while prohibiting it in specified circumstances. The primary purpose of indemnification is to provide assurance to those prepared to become corporate directors that they will be recompensed for any adverse consequences arising from well-intentioned entrepreneurism undertaken on the corporation's behalf. This assurance serves to attract and to protect competent directors who will advance the interests of the corporation.

24 However, to encourage appropriate conduct, Parliament and the provincial legislatures also provide deterrents against misconduct. Arguably, the most effective deterrent is the consequence, including the stigma, of director prosecution and conviction. Another deterrent is the legislative prohibition against corporate indemnification for director misconduct. [1]

25 This tension between the competing objectives of encouraging director entrepreneurism on the one hand, and discouraging director misconduct on the other, informs the interpretation of s. 124(3).

The Onus and the Test

26 From the perspective of these competing objectives, I turn to the wording of s. 124(3) of the CBCA. Section 124(3) requires a consideration of the particular context in which the individual acted. Subsection 124(3)(a) sets out, as a pre-condition to indemnification, that the individual must have acted honestly and in good faith in the best interests of the corporation. Section 124(3)(b) adds an additional prerequisite regarding indemnification arising from criminal or regulatory penalties: the individual must also have had reasonable grounds for believing his or her conduct was lawful.

27 In keeping with the contextual perspective, Parliament determined that entitlement to indemnification must be decided on the basis of the circumstances that existed at the time of the director's (a) conduct and (b) belief. This is clear not only from the wording of s. 124(3), but also from the leading case of *Blair v. Consolidated Enfield Corp.*, [1995] 4 S.C.R. 5 (S.C.C.), where Iacobucci J. observed, at para. 74, that the similar non-indemnification provision in the *Business Corporations Act*, R.S.O. 1990, c. B.16, allows "for reimbursement for reasonable good faith behaviour, thereby discouraging the hindsight application of perfection."

28 In addressing the required degree of misconduct, Iacobucci J. instructed, at para. 74, that indemnification will only be prohibited if the director acted with *mala fides*. At para. 35, he cited *General Motors of Canada Ltd. v. Brunet* (1976), [1977] 2 S.C.R. 537 (S.C.C.), at p. 548, for the proposition that "persons are assumed to act in good faith unless proven otherwise" and placed the onus of proving *mala fides* on the corporation opposing indemnification.

29 Noting that this interpretation of s. 124(3)(a) is in keeping with academic commentary, Iacobucci J. quoted, at para. 74, from Jacob S. Ziegel *et al.*, *Cases and Materials on Partnerships and Canadian Business Corporations*, 3d ed., vol. 1 (Scarborough, Ont.: 1994), at p. 523. There, the authors acknowledge the appropriateness of denying indemnification for "fraud or misappropriation", but recognize that a director should not be denied indemnification if the "conduct ... was not coloured by any opportunistic behaviour". Opportunistic or self-seeking behaviour may be encompassed within the term *mala fides* because such behaviour exhibits a type of dishonesty that should not be countenanced by an award for indemnification.

30 The scope of the bad faith described in *Blair* was clarified in *Entreprises Sibeca inc. c. Frelighsburg (Municipalité)*, [2004] 3 S.C.R. 304 (S.C.C.). At para. 25, Deschamps J., writing for the court and citing *McCullock Finney c. Barreau (Québec)*, [2004] 2 S.C.R. 17 (S.C.C.) at para. 39, accepted that bad faith can encompass recklessness in the sense that the conduct at issue is so inexplicable that it suggests an absence of good faith. Deschamps J. also noted, at para. 26, that this clarification means "no more than the admission in evidence of facts that amount to circumstantial evidence of bad faith where a victim is unable to present direct evidence of it." Thus, inexplicable, apparently reckless, conduct may lead to the inference that the conduct was deliberate, intentional and undertaken in bad faith.

31 Since the dispute in *Blair* involved a director's indemnification for a civil proxy dispute, it did not expressly consider the second branch of the CBCA's non-indemnification test under s. 124(3)(b), which requires reasonable grounds for belief in lawful conduct.

32 Nonetheless, in my view, for reasons analogous to the observation in *Blair* regarding honest and good faith conduct, the corporation also bears the burden of showing that the director did not have reasonable grounds for his or her belief that the conduct was lawful. Placing the burden on the corporation is consistent with the principle affirmed in *Blair* regarding s. 124(3)(a) that persons are assumed to act in good faith. In my view, under s. 124(3)(b), persons should also be assumed to believe they are acting lawfully and to have reasonable grounds for that belief, unless the contrary is proven. There is no indication in the wording of the legislation that suggests a different burden should be imposed for (b) than for (a). The imposition of the burden on the corporation best balances the promotion of strong director decision-making, on the one hand, while discouraging irresponsible behaviour on the other. Finally, as a practical matter, this placement of the burden makes sense because the corporation, and not the individual director, will most likely have the advantage of unrestricted access to corporate documents relevant to the indemnification proceeding.

33 Relying on *Catalyst Fund General Partner I Inc. v. Hollinger Inc.* (2006), 79 O.R. (3d) 288 (Ont. C.A.), BEI submits that an objective test must be applied in determining whether Bennett satisfied s. 124(3)(a) and that the application judge erred in applying a subjective standard.

34 In *Catalyst*, Cronk J.A., writing for the panel, determined, at para. 105, that a director was not entitled to indemnification under s. 124(3) because the significance of the changed circumstances "would have been apparent to even the most untrained observer". Thus, she concluded, at para. 106, the director "cannot make out a claim for indemnification by relying on an unreasonable subjective belief."

35 In my view, *Catalyst* rightly concluded that a director cannot ground a claim for indemnification on an unreasonable belief where that belief would have been obviously erroneous to even the most untrained observer. Such a belief would be analogous to the reasoning in *Enterprises* that observed that a director cannot rely on recklessness to defend otherwise indefensible conduct. Thus, the conclusion in *Catalyst* reflects the finding that the director's evidence regarding his good faith was not credible in the circumstances of that case. Accordingly, I do not accept the appellant's submission that *Catalyst* changed the test from that set out in *Blair*, as clarified in *Enterprises*.

36 Indeed, the *Blair* reasonableness test achieves the same result by asking whether the director acted reasonably when the director's conduct or belief is considered in the context of the perspective of a director in comparable circumstances at the time. Looking at comparable circumstances involves looking at the issue from the perspective of the knowledge and skill set of the individual director and the information and advice upon which the director's conduct or belief was based.

37 The wording employed by Parliament in both s. 124(3)(a) and (b) supports this interpretation of the reasonableness test. That wording instructs that the question is whether "the individual" exhibited good faith conduct and had reasonable grounds for believing that his or her conduct was lawful. The answer must include consideration of the context in which the director decided on the conduct or formed the belief at issue. It is implicit in the wording that the conduct or belief at issue must have been reasonable when considered in context.

38 I turn to the application of the test to the circumstances of this case, an issue that I approach mindful of the factual findings made by the application judge.

Application of the test

39 By admitting to breaches of s. 122(1)(b) and s. 122(3) of the *Securities Act*, Bennett acknowledged to the OSC that, at the time, the Contract dispute was a material change that BEI was obliged to disclose. However, BEI acknowledges that this admission does not, in itself, preclude Bennett's indemnification. Otherwise, there would be no point in the CBCA's provision of director indemnification for such administrative penalties. Moreover, the onus and test regarding an offence under the *Securities Act* differ from the onus and test mandated by the non-indemnification provisions of the CBCA. Thus, while Bennett's admissions to the OSC may reflect on the credibility of his evidence before the application judge, the OSC findings do not predetermine the result of the indemnification application.

40 Both before the OSC and on his application, Bennett attested that, in the light of all the circumstances, he mistakenly believed the Contract dispute would be resolved in BEI's favour and so he did not consider the ongoing developments to be a change in the binding nature of the Contract, let alone a material one. For this reason, he did not identify any obligation to disclose. Thus, he argues, he acted honestly in BEI's interests and that he believed his conduct was lawful. Further, he asserts there is no basis on which to conclude his belief or conduct was reckless or that his view would have been obviously erroneous to even the most untrained observer at the time.

Section 124(3)(a)

41 Under s. 124(3)(a), the issue for the application judge was whether BEI had established that Bennett was not credible in his evidence that he had "acted honestly and in good faith with a view to the best interests of the corporation".

42 While the application judge was alive to BEI's position that Bennett was lying about his good faith conduct (or that he acted unreasonably), he concluded that BEI had failed to satisfy its onus to disprove Bennett's evidence. BEI argues that the application judge erred in so concluding. I do not agree.

43 While undoubtedly the obligation to disclose a material change is absolute, it is not always clear at the time that an event, or even a series of events, constitutes a material change. Such a determination may turn on an assessment of the reliability of the available information. In this case, Bennett gave reasons why he did not take the developing information seriously at the time. Those reasons included the assurances about the Contract Bennett received from BEI's own U.S. representative

and from Sevenson's representative. Bennett also had regular discussions about the Contract with another director who was a lawyer. In addition, Bennett had discussions with his fellow director on the Disclosure Committee, albeit those discussions were not couched in terms of any disclosure obligations since he did not consider the developments to constitute a material change. Bennett's evidence was further supported by his open discussions with other officers and directors at BEI and the candid discussions with the Board about the dispute. In other words, Bennett's belief was an informed one.

44 Furthermore, the honesty of Bennett's belief was supported by the absence of any motive to withhold disclosure. Indeed, Bennett pressed the BEI Board to proceed with the development of a new plant that would only have been required to honour the Contract. Bennett would not likely have done so if he believed the Contract was in jeopardy. Moreover, unlike others involved in BEI, Bennett did not stand to gain personally from the non-disclosure. This is also evident from Bennett's election to take his bonus in options and from his decision not to sell any BEI stock.

45 Based on this evidence, the application judge concluded that he was not able to reject Bennett's position. From reading the application judge's reasons as a whole, it is clear that BEI failed to establish that Bennett's stated belief was either opportunistic or amounted to a reckless disregard of his obligations. The application judge specifically observed the absence of "conclusive objective evidence on which to make such a finding." He considered and applied Iacobucci J.'s reasoning at para. 76 of *Blair*:

> It is insufficient to say retrospectively that Blair 'should have' acted differently or that he did not handle things perfectly in order to deny indemnification under s. 136(1). Actual *mala fides* must be shown such that the director did not act with a view to the best interests of the corporation.

Similarly, it is not enough in this case to say, with the benefit of hindsight, that Bennett should have done more. The application judge accordingly was entitled to conclude that BEI had not satisfied the burden of establishing that Bennett acted in bad faith.

Section 124(3)(b)

46 The trial judge did not expressly separate his consideration of the s. 124(3)(b) requirement that Bennett had reasonable grounds to believe that non-disclosure was lawful from his s. 124(3)(a) analysis. The two requirements are distinct: see *People's Department Stores Ltd. (1992) Inc., Re*, [2004] 3 S.C.R. 461 (S.C.C.), at para. 33, where Major and Deschamps JJ. discuss this distinction in the context of the different duties of directors under s. 122(1) of the CBCA.

47 Nonetheless, the application judge's reasons demonstrate that he was alive to the distinction between s. 124(3)(a) and (b). On more than one occasion, he referred to "belief in lawful conduct" as a requirement that was in addition to the requirement of honesty and good faith. Moreover, in the particular circumstances of this case, it is apparent that the facts and the evidence underpinning both branches of the test, to a certain extent, are intertwined, as are the arguments advanced by the appellant.

48 One of BEI's arguments, which applies to both branches of the test, is that Bennett could not possibly have had reasonable grounds to believe that his conduct was lawful (or that he was acting in good faith) when he did not consult legal counsel.

49 This issue arose in *Blair* where, unlike in this case, the director seeking indemnification relied on the fact that he had consulted counsel before proceeding with the impugned conduct as evidence that he had acted in good faith, In upholding an order for indemnification, Iacobucci J. explained, at paras. 58 and 65, that, while a director's *de facto* reliance on legal advice does not guarantee indemnification, reliance on counsel's advice "will strongly militate *against* a finding of *mala fides* or fiduciary breach" (emphasis in original). The court in *Blair* relied on several additional considerations in ultimately concluding that the director was entitled to indemnification.

50 In my view, while reliance on reasonable legal or professional advice will substantially assist a director seeking indemnification in establishing reasonable grounds for belief that his or her conduct is lawful, such consultation is not a prerequisite to indemnification. Rather, the variety of additional considerations that may come into play in a particular case makes it both undesirable and unnecessary to promulgate an inflexible rule mandating legal advice as a prerequisite to indemnification under either branch of s. 124(3).

51 That said, however, a failure to obtain professional advice may raise questions in a particular case about a director's conduct or belief. In such a case, it may be necessary to assess the surrounding circumstances and conduct of the director at the relevant time to look for other evidence of the reasonableness of the relied-upon belief.

52 In this case, Bennett testified that he did not turn his mind to the issue of disclosure or seek legal advice because it simply did not occur to him to do so, in part, because he was an engineer and not a lawyer. Standing on its own, this explanation cannot constitute reasonable grounds under s. 124(3)(b). A director serving on a Disclosure Committee, lawyer or not, is expected to have at least a basic familiarity with disclosure obligations.

53 However, this was not a case where Bennett recognized and wilfully ignored an evident disclosure obligation or failed to make reasonable inquiries. To the contrary, as detailed above, the evidence shows that Bennett sought information from BEI's U.S. representative and from Sevenson's representative. He also had discussions with other directors and officers in the company. While Bennett was subsequently proven wrong in his decision not to make earlier disclosure, BEI failed to demonstrate that, from the perspective of someone in Bennett's position at the time, Bennett did not have reasonable grounds for believing he was acting lawfully.

54 While the application judge's reasons are couched in terms of Bennett's belief in the continued validity of the Contract, rather than in terms of his belief that he did not have disclosure obligations, in the circumstances of this case, the two beliefs are synonymous. If Bennett honestly and reasonably believed the Contract was not in jeopardy, and that it accordingly remained a binding contract, there was no basis upon which he ought to have believed that he was obliged to make disclosure of a material change. I see no error of law in the application judge's reasons and therefore no basis to interfere with his conclusions in this regard.

55 Accordingly, I conclude that it was open to the application judge to determine that BEI did not meet the onus on it to establish that Bennett did not have reasonable grounds to believe his conduct was lawful.

56 Finally, I note that this is not a case that invokes the business judgment rule discussed in *Kerr v. Danier Leather Inc.*, [2007] 2 S.C.R. 331 (S.C.C.). In *Kerr*, Binnie J. instructed, at para. 54, that the business judgment rule "is a concept well-developed in the context of *business* decisions but should not be used to qualify or undermine the duty of disclosure" under the *Securities Act* (emphasis in original) Accordingly, the test to be met in this case is that set out in s. 124(3) of the CBCA.

Other errors

57 BEI also submits that the application judge made factual errors. I reject this ground of appeal. To the extent that BEI argues that the application judge was obliged to refuse indemnification in the light of the factual findings of the OSC, I disagree. I have already given my view that the different burden and test under the *Securities Act* and the CBCA may result in different outcomes. I also disagree with BEI's characterization of the application judge's reasons as requiring expert or other evidence to refute Bennett's evidence. While this issue is more a question of law than of fact, in my view, the application judge's excerpted reasons do no more than reinforce his already-stated view that the evidence led by BEI was insufficient to meet the requisite onus under either branch of the s. 124(3) test.

58 Finally, BEI observes that the OSC specifically declined to impose a penalty on BEI on the basis that such a penalty would ultimately be borne by the shareholders. From this, the appellant argues that granting Bennett indemnification in this application would impose the financial burden on the shareholders, contrary to the OSC's intention.

59 In my view, BEI's argument is answered in two ways. First, while the argument is premised on the assumption that Bennett's conduct was sufficiently egregious to deny him indemnification, the application judge concluded that BEI failed to prove such misconduct and, as I have already stated, I see no reason to interfere with his conclusion. Second, BEI chose to protect directors against the imposition of financial penalties by enacting a by-law providing for director indemnification except in the case of misconduct. Again, as found by the application judge, BEI has failed to prove such misconduct.

Result

60 In the result, I would dismiss the appeal. I would also award costs to Bennett fixed at $14,000, inclusive of disbursements and GST.

***R.G. Juriansz J.A.*:**

I agree.

***G. Epstein J.A.*:**

I agree.

Appeal dismissed.

Footnotes

1 The relevant statute in every province permits indemnification generally, and restricts it in specified circumstances. Indeed, most of the provincial indemnification provisions prescribe the identical good faith and lawful conduct requirements set out in the CBCA (New Brunswick, Newfoundland, Ontario, Manitoba, Alberta, Saskatchewan, and British Columbia), and others deny indemnification where the charges, expenses, or liability were occasioned by the director's own fault (Quebec), wilful neglect of default (Prince Edward Island), or dishonesty (Nova Scotia): see *Companies Act*, R.S.P.E.I. 1988, c. C-14, s. 64; *Business Corporations Act*, S.N.B. 1981, c. B-9.1, s. 81; *Companies Act*, R.S.N.S. 1989, c. 81, ss. 204 and 205; *Corporations Act*, R.S.N.L. 1990, c. C-36, s. 205; *Companies Act*, R.S.Q. c. C-38, ss. 90 and 184; *Business Corporations Act*, R.S.O. 1990, c. B.16, s. 136; *Corporations Act*, C.C.S.M. c. C225, s. 119; *Business Corporations Act*, R.S.A. 2000, c. B-9, s. 124; *Business Corporations Act*, R.S.S. 1978, c. B-10, s. 119; and, *Business Corporations Act*, [SBC 2002] c. 57, s. 163.

Liability of directors
113(1) Directors of a corporation who vote for or consent to a resolution authorizing the issue of a share under section 25 for a consideration other than money are jointly and severally liable to the corporation to make good any amount by which the consideration received is less than the fair equivalent of the money that the corporation would have received if the share had been issued for money on the date of the resolution.

Further liability of directors
113(2) Directors of a corporation who vote for or consent to a resolution authorizing

(a) a purchase, redemption or other acquisition of shares contrary to section 32, 33 or 34;

(b) a commission, contrary to section 39;

(c) a payment of a dividend contrary to section 40;

(d) [repealed] S.M. 2006, c. 10, s. 14;

(e) a payment of an indemnity contrary to section 119;

(f) a payment to a shareholder contrary to section 184 or 234; or

(g) any investment or financial assistance contrary to the provisions of Part XXIV;

are jointly and severally liable to restore to the corporation any amounts so distributed or paid and not otherwise recovered by the corporation.

Contribution
113(3) A director who has satisfied a judgment rendered under this section is entitled to contribution from the other directors who voted for or consented to the unlawful act upon which the judgment was founded.

Responsabilité des administrateurs
113(1) Les administrateurs qui, par vote ou acquiescement, approuvent l'adoption d'une résolution autorisant l'émission d'actions conformément à l'article 25, en contrepartie d'un apport autre qu'en numéraire, sont conjointement et individuellement tenus de donner à la corporation la différence entre la juste valeur de cet apport et celle de l'apport en numéraire qu'elle aurait dû recevoir à la date de la résolution.

Responsabilité supplémentaire des administrateurs
113(2) Les administrateurs qui ont, par vote ou acquiescement, approuvé l'adoption d'une résolution autorisant :

a) l'acquisition, notamment par achat ou rachat, d'actions en violation de l'article 32, 33 ou 34;

b) le versement d'une commission en violation de l'article 39;

c) le versement d'un dividende en violation de l'article 40;

d) [abrogé] L.M. 2006, c. 10, art. 14;

e) le versement d'une indemnité en violation de l'article 119;

f) le versement de sommes à des actionnaires en violation de l'article 184 ou 234;

g) un placement ou une aide financière en violation des dispositions de la partie XXIV,

sont conjointement et individuellement tenus de restituer à la corporation les sommes en cause non encore recouvrées.

Répétition
113(3) L'administrateur qui a satisfait au jugement rendu en vertu du présent article peut répéter les parts des administrateurs qui ont, par vote ou acquiescement, approuvé l'adoption de la mesure illégale en cause.

(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.

b) de nommer un administrateur à un poste quelconque;

c) pour la même personne, d'occuper plusieurs postes.

Duty of care of directors and officers
117(1) Every director and officer of a corporation in exercising his powers and discharging his 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.

Devoir des administrateurs et dirigeants
117(1) Les administrateurs et les dirigeants doivent, dans l'exercice de leurs fonctions, agir :

a) avec intégrité et de bonne foi au mieux des intérêts de la corporation;

b) avec soin, diligence et compétence, comme le ferait en pareilles circonstances une personne avisée.

Duty to comply
117(2) Every director and officer of a corporation shall comply with this Act and the regulations, the articles and by-laws, and any unanimous shareholder agreement.

Observation
117(2) Les administrateurs et les dirigeants doivent observer la présente loi, ses règlements d'application, les statuts, les règlements administratifs ainsi que les conventions unanimes des actionnaires.

No exculpation
117(3) Subject to subsection 140(5), no provision in a contract, the articles, the by-laws or a resolution relieves a director or officer from the duty to act in accordance with this Act or the regulations or relieves him from liability for a breach thereof.

Absence d'exonération
117(3) Sous réserve du paragraphe 140(5), aucune disposition d'un contrat, des statuts, des règlements administratifs ou d'une résolution ne peut libérer les administrateurs ou les dirigeants de l'obligation d'agir conformément à la présente loi et à ses règlements d'application ni des responsabilités découlant de cette obligation.

Interpretation
117(4) This section is in addition to and not in derogation of, any enactment or rule of law relating to the duty or liability of directors or officers of a corporation.

S.M. 1988-89, c. 11, s. 5.

Interprétation
117(4) Le présent article s'ajoute et ne déroge pas aux textes législatifs ou aux règles de droit concernant les obligations et les responsabilités des administrateurs ou des dirigeants.

L.M. 1988-89, c. 11, art. 5.

Dissent
118(1) A director who is present at a meeting of directors or committee of directors is deemed to have consented to any resolution passed or action taken thereat, unless

Dissidence
118(1) L'administrateur présent à une réunion du conseil ou d'un comité de celui-ci est réputé avoir acquiescé à toutes les résolutions adoptées ou à toutes les mesures prises, sauf dans l'un ou l'autre des cas suivants :

Defence of good faith
118(5) A director has complied with his or her duties under subsection 117(1) if the director relied in good faith on financial statements or a report described in clause (4)(a) or (b).

S.M. 2006, c. 10, s. 16.

Bonne foi
118(5) L'administrateur s'est acquitté des devoirs imposés au paragraphe 117(1) s'il s'appuie de bonne foi sur les états financiers ou les rapports visés à l'alinéa (4)a) ou b).

L.M. 2006, c. 10, art. 16.

Indemnification
119(1) Except in respect of an action by or on behalf of the corporation or body corporate to procure a judgment in its favour, a corporation may indemnify a director or officer of the corporation, a former director or officer of the corporation or a person who acts or acted at the corporation's request as a director or officer of a body corporate of which the corporation is or was a shareholder or creditor, and his heirs and legal representatives, against all costs, charges and expenses, including an amount paid to settle an action or satisfy a judgment, reasonably incurred by him in respect of any civil, criminal or administrative action or proceeding to which he is made a party by reason of being or having been a director or officer of the corporation or body corporate, if

(a) he acted honestly and in good faith with a view to the best interests of the corporation; and

(b) in the case of a criminal or administrative action or proceeding that is enforced by a monetary penalty, he had reasonable grounds for believing that his conduct was lawful.

Indemnisation
119(1) La corporation peut indemniser ses administrateurs, ses dirigeants ou leurs prédécesseurs, les personnes qui, à sa demande, agissent en cette qualité pour une personne morale dont elle est actionnaire ou créancière ainsi que leurs héritiers et représentants légaux, de tous leurs frais et dépenses raisonnables, y compris les sommes versées pour transiger sur un procès ou exécuter un jugement, occasionnés lors de poursuites civiles, criminelles ou administratives auxquelles ils étaient parties en cette qualité, à l'exception des actions intentées par la corporation ou la personne morale, ou pour leur compte, en vue d'obtenir un jugement favorable, si :

a) d'une part, ils ont agi avec intégrité et de bonne foi au mieux des intérêts de la corporation;

b) d'autre part, dans le cas de poursuites criminelles ou administratives aboutissant au paiement d'une amende, ils avaient de bonnes raisons de croire que leur conduite était conforme à la loi.

Indemnification in derivative actions
119(2) A corporation may with the approval of a court indemnify a person referred to in subsection (1) in respect of an action by or on behalf of the corporation or body corporate to procure a judgment in its favour, to which he is made a party by reason of being or having been a director or an officer of the corporation or body corporate, against all costs, charges and expenses reasonably incurred by him in connection with the action if he fulfils the conditions set out in clauses (1)(a) and (b).

Indemnisation lors d'actions indirectes
119(2) La corporation peut, avec l'approbation du tribunal, indemniser les personnes visées au paragraphe (1) des frais et dépenses raisonnables résultant du fait qu'elles ont été parties à des actions intentées par la corporation ou par une personne morale, ou pour leur compte, en vue d'obtenir un jugement favorable si elles remplissent les conditions énoncées aux alinéas (1)a) et b).

Indemnity as of right
119(3) Notwithstanding anything in this section, a person referred to in subsection (1) is entitled to indemnity from the corporation in respect of all costs, charges and expenses reasonably incurred by him in connection with the defence of any civil, criminal or administrative action or proceeding to which he is made a party by reason of being or having been a director or officer of the corporation or body corporate, if the person seeking indemnity

(a) was substantially successful on the merits in his defence of the action or proceeding; and

(b) fulfils the conditions set out in clauses (1)(a) and (b).

Droit à indemnisation
119(3) Malgré le présent article, les personnes visées au paragraphe (1) peuvent demander à la corporation de les indemniser de leurs frais et dépenses raisonnables à l'occasion des actions civiles, criminelles ou administratives auxquelles elles étaient parties en raison de leurs fonctions, dans la mesure où :

a) d'une part, elles ont obtenu gain de cause sur la plupart de leurs moyens de défense au fond;

b) d'autre part, elles remplissent les conditions énoncées aux alinéas (1)a) et b).

Directors' and officers' insurance
119(4) A corporation may purchase and maintain insurance for the benefit of any person referred to in subsection (1) against any liability incurred by him

(a) in his capacity as a director or officer of the corporation, except where the liability relates to his failure to act honestly and in good faith with a view to the best interests of the corporation; or

(b) in his capacity as a director or officer of another body corporate where he acts or acted in that capacity at the corporation's request, except where the liability relates to his failure to act honestly and in good faith with a view to the best interests of the body corporate.

Assurance des administrateurs ou dirigeants
119(4) La corporation peut souscrire au profit des personnes visées au paragraphe (1) une assurance couvrant la responsabilité qu'elles encourent :

a) soit pour avoir agi en qualité d'administrateur ou de dirigeant de la corporation, à l'exception de la responsabilité découlant du défaut d'agir avec intégrité et de bonne foi au mieux des intérêts de la corporation;

b) soit pour avoir, sur demande de la corporation, agi en qualité d'administrateur ou de dirigeant d'une autre personne morale, à l'exception de la responsabilité découlant du défaut d'agir avec intégrité et de bonne foi au mieux des intérêts de la personne morale.

Application to court
119(5) A corporation or a person referred to in subsection (1) may apply to a court for an order approving an indemnity under this section and the court may so order and make any further order it thinks fit.

Demande au tribunal
119(5) Le tribunal peut, par ordonnance, approuver, à la demande de la corporation ou de l'une des personnes visées au paragraphe (1), toute indemnisation prévue au présent article, et prendre toute autre mesure qu'il estime pertinente.

Notice to director
119(6) An applicant under subsection (5) shall give the Director notice of the application, and the Director is entitled to appear and be heard in person or by counsel.

Avis au directeur
119(6) L'auteur de la demande prévue au paragraphe (5) doit en aviser le directeur; celui-ci peut comparaître en personne ou par l'intermédiaire d'un avocat.

Other notice
119(7) Upon an application under subsection (5), the court may order notice to be given to any interested person and that person is entitled to appear and be heard in person or by counsel.

Remuneration
120 Subject to the articles, the by-laws and any unanimous shareholder agreement, the directors of a corporation may fix the remuneration of the directors, officers and employees of the corporation.

Autre avis
119(7) Sur demande présentée en vertu du paragraphe (5), le tribunal peut ordonner qu'avis soit donné à tout intéressé; celui-ci peut comparaître en personne ou par l'intermédiaire d'un avocat.

Rémunération
120 Sous réserve des statuts, des règlements administratifs et de toute convention unanime des actionnaires, les administrateurs peuvent fixer leur propre rémunération ainsi que celle des dirigeants et des employés de la corporation.