FEBRUARY 2009

Blaney McMurtry
BARRISTERS & SOLICITORS LLP

Commercial Litigation Update

This newsletter is designed to bring news of changes to the law, new law, interesting decisions and other matters of interest to our commercial litigation clients and friends. We hope you will find it interesting, and welcome your comments.

Feel free to contact any of the lawyers who wrote or are quoted in these articles for more information, or call the head of our Commercial Litigation group, Lou Brzezinski at 416.593.2952 or lbrzezinski@blaney.com

IN THIS ISSUE:

Creditors' Relief Act Can Speed Up Recovery of Bad Debt
Chad Kopach

Canada's ABCP Crisis - The Aftermath
Lou Brzezinski

Partnership Agreements - They Can Save You Heartache
John Polyzogopoulos

Speaking Engagements

The CRA can provide creditors with a simpler, quicker, and more economic legal approach for recovering debts.

CREDITORS' RELIEF ACT CAN SPEED UP RECOVERY OF BAD DEBT

Chad Kopach

Legal action to collect an overdue debt is unfortunate but sometimes necessary in business and in life.

Creditors who have run out of options in their efforts to collect what they are owed may hesitate to sue because of the time, effort and expense that they fear will be involved.

Such creditors will be interested to know that, in their particular situations, there may be a simpler, quicker and more economic legal approach.

Such an approach is offered by the *Creditors' Relief Act* (the "CRA"). It is available to both Canadian and foreign creditors who are trying to collect from Ontario debtors who have already been sued successfully by somebody else, who have not "paid up" (or "satisfied" the judgements against them) and where such unsatisfied judgements are registered with the sheriff.

In these situations, the CRA allows the creditor to "piggyback" on successful suits that have already been conducted against the debtor. Sections 6 to 13 of the CRA allow the creditor to deliver to the debtor a short affidavit of claim and notice of claim. If the debtor does not deliver notice, within 10 days of service, that it contests the claim, the creditor can obtain a certificate from the court. The certificate is then registered with the sheriff. After registration, if the sheriff receives any funds (for example, as a result of other judgment creditors' collection efforts), the creditor shares in the distribution on a pro-rated basis.

This procedure under the CRA can result in a "judgment" registered with the sheriff in one-third of the time compared to proceeding by way of a regular action (that is, by Statement of Claim or Notice of Application).

The CRA can also be an effective tool for enforcing foreign judgments.

If a creditor has a judgment from a Canadian province or territory (other than Quebec), or from the United Kingdom, the judgment can be recognized in Ontario, which has reciprocal enforcement agreements with these other jurisdictions.

However, if a creditor has a judgment from another jurisdiction in the world, the Ontario court will not recognize it as an Ontario judgment. The usual method of enforcing this foreign judgment will be to sue as a debt. In other words, the judgment creditor will have to start a new action or application.

COMMERCIAL LITIGATION UPDATE

"Three important developments have occurred since the Supreme Court of Canada refused to hear an appeal from the Court of Appeal for Ontario dealing with the plan to restructure third-party ABCP(asset-backed commercial paper)."

Chad Kopach is a member of Blaneys commercial litigation practice and also does general civil litigation. Much of his practice involves collection actions in the architecture, construction and financial services areas. In addition, he represents clients in professional negligence actions. Chad is a member of The Advocates' Society, the Ontario Bar Association and the Toronto Construction Association.

Chad may be reached directly at 416.593.2985 or ckopach@blaney.com.

This is where the CRA is at its most effective. If the debtor in question has an execution registered against it in Ontario, the CRA permits the foreign creditor to deliver the affidavit of claim and notice of claim. If 10 days pass without the debtor contesting the claim in the prescribed form, the foreign judgment creditor can obtain a certificate and register it with the sheriff. Using this process, the foreign judgment creditor will share in the distribution with the other judgment creditors, but without the bother of having to begin a new action (or application) and prosecute the matter to judgment. ■

CANADA'S ABCP CRISIS - THE AFTERMATH

Lou Brzezinski

An award-winning background article describing and explaining the Canadian experience in the global credit crisis, the role played by asset-backed commercial paper (ABCP), and Canada's management of the crisis here through a court-approved plan to restructure the ABCP market, was published in the October, 2008 issue of Commercial Litigation Update. *That article, written by Lou Brzezinski, who leads Blaney McMurtry's commercial litigation group, began as follows:*

"The credit crisis that has affected Canada, the United States, and the rest of the world in recent months has its roots in an esoteric financial market known as asset-backed commercial paper (ABCP).

"The collapse of this market effectively removed hundreds of billions of dollars of assets from financial institutions in North America. The loss of these assets essentially prevented financial institutions from borrowing money at the same interest rate, or in the same quantity, as they did before. In addition, U.S. banks that had chosen to inject an inordinate portion of their investment capital into these assets found themselves unable to meet their own debt obligations to other financial institutions, and soon either sought protection from their creditors under the U.S. Bankruptcy Code Chapter 7 and Chapter 11, or were gobbled up by their creditors, or were rescued by large cash injections by the U.S. government.

"The Canadian approach to this crisis was far different. Through a negotiated consensus, the stakeholders in Canada reached a standstill agreement which ultimately was incorporated into a court order. As a result, the fallout in Canada from this market failure was relatively inconsequential."

In this issue of Commercial Litigation Update, *Mr. Brzezinski writes about developments since.*

Three important developments have occurred since the Supreme Court of Canada refused to hear an appeal from the Court of Appeal for Ontario dealing with the plan to restructure third-party ABCP.

First, the Pan Canadian Investors' Committee, which was established to restructure the ABCP market, was compelled by market forces to seek financial assistance from the federal and provincial Governments so as to implement the restructuring plan for the third party ABCPs.

Second, the Investment Industry Regulatory Organization of Canada (IIROC), the national, self-regulator that oversees all investment dealers

COMMERCIAL LITIGATION UPDATE

"Despite the fact that the Supreme Court of Canada paved the way for the implementation of the plan proposed by the Pan Canadian Committee, by mid-December 2008, the plan had yet to be implemented."

Lou Brzezinski is a Blaney McMurtry partner and leader of the firm's Commercial Litigation Group. He has been actively involved in all aspects of Commercial Litigation and Insolvency, has argued before all levels of courts and tribunals, has acted on behalf of Trustees and Receivers, and has been involved in major Canadian bankruptcies, including Stelco, Air Canada, Eaton's and Hy & Zel's.

Lou may be reached directly at 416.593.2952 or lbrzezinski@blaney.com

and trading activities in Canada's debt and equity marketplaces, issued a report as to the manner, process and role that investment dealers played in the ABCP freeze-up. The IIROC report clearly pointed a finger at its own dealer members in contributing and assisting in the ABCP crisis.

Third, an expert panel on securities regulation in Canada was struck and a report was delivered to the Minister of Finance by Thomas Hockin, Chair of the expert panel. The Hockin Report recommended the establishment of a National Canadian Securities Commission which would have control over all capital markets, and further recommended the regulation of exchange-traded derivatives and over-the-counter derivatives.

The ABCP Restructuring Plan

Despite the fact that the Supreme Court of Canada paved the way for the implementation of the plan proposed by the Pan Canadian Committee, by mid-December 2008, the plan had yet to be implemented.

The main hurdle this time was the rising turmoil in the financial markets, which caused credit spreads to move apart to record levels. As a result, approximately $18 billion had to in place in a margin pool to support leverage credit default swaps. This was $4.5 billion more than the original plan proposed.

Once again, Purdy Crawford, the committee's distinguished chair, was able to broker a deal among the governments of Canada, Quebec, Ontario and Alberta to make the additional $4.5 billion available.

The plan would see small investors holding less than $1 million of ABCP receive refunds immediately. The original ABCP notes of all classes and kinds have now been converted to approximately 157 different classes of notes. The bulk of them mature at the end of 2016. These notes have been rated by the Dominion Bond Rating Service between A to top-rated AAA.

Experts say that while there is no secondary market for the new notes yet, a seller, at present, would likely get between 25 cents and 50 cents on the dollar for most of them.

The final touches of this plan, with its amendments, was approved January 16, 2009 by Mr. Justice Colin Campbell of the Ontario Superior Court of Justice. (It was Mr, Justice Campbell who approved the original Pan-Canadian Investor's Committee plan last June 8.)

The IIROC Report

This report that was published by the independent investment dealers came up with a series of findings after its investigation in October of 2008. The general findings were that third party ABCPs were issued under the same securities law exemptions that were intended for traditional commercial paper. These prospectus and registration exemptions were recently made uniform across Canada and required an "approved credit rating" from their approved credit rating organization in lieu of minimum purchase amounts.

Because of confidentiality agreements with sponsors, there was no transparency as to the underlying assets or quality and performance of the portfolio.

In the survey, of 21 investment firms, it was found that none had put third party ABCP through their product due diligence process. The reasons given were:

"(The Hockin Report) essentially pointed out that the lack of a national Canadian securities regulator has raised concerns about systemic risk, as there is no national entity accountable for the stability of Canada's national markets."

1. They did not view third party ABCP as a new product and did not distinguish between bank-sponsored ABCP and third party ABCP.

2. Most dealer members relied exclusively on the DRBS rating of R1.

3. They viewed third party ABCPs as cashable money market instruments that had obtained the highest possible credit rating.

4. None of the firms interviewed reported referring any marketing materials for general distribution to its clients or sales personnel.

5. Dealer members interviewed were not worried that third-party ACBP might be unsuitable for clients because they viewed it as a cashable money market instrument with a high credit rating.

6. No dealer member reported providing any training or special written materials to registered representatives, supervisors or compliance staff regarding third party ABCPs.

Canadian-style liquidity triggered only by market interruption was different than global-style liquidity guarantees. It was the Canadian-style liquidity guarantee that prevented the rating agencies in the U.S.A. from providing any rating whatsoever to the Canadian ABCP.

The Dominion Bond Rating Service (DBRS) which provided a rating was the only credit rating agency for third party ABCP programs in Canada.

The fact that three U.S.A. bonding agencies refused to even rate the Canadian ABCP financial instrument because of its liquidity provision should have been a red flag to the dealers to undertake a thorough and complete investigation of this market.

These findings shine a light on what appears to be a murky, unregulated, and, in large part, misunderstood financial investment vehicle. The fact that investment dealers throughout Canada seem to have paid little or no attention to the underlying assets of the ABCP instruments emphasizes the importance of the releases from potential findings of liability of officers, directors and financial institutions involved in the ABCP market which form part of the plan of compromise under the *Companies Creditors' Arrangement Act* order regarding the ABCP market.

It is self-evident that if the investment dealers' own self-regulatory body found there to be significant deficiencies in the practice and process of marketing ABCP to retail clients, then it would be clear that in a court of law, there would most probably be a good chance that there would be findings of liability on the part of these investment dealers to any individuals who were advised to get into the ABCP market without the proper and requisite disclosure.

The Hockin Report

Yet a further response took place on January 8, 2009, when the expert panel on securities regulation published its findings. The committee was chaired by the Honourable Thomas Hockin, the former federal cabinet minister and CEO of the Investment Funds Institute of Canada. This report essentially pointed out that the lack of a national Canadian securities regulator has raised concerns about systemic risk, as there is no national entity accountable for the stability of Canada's national markets. As the ABCP financial crisis had indicated, systemic risk is no longer to be confined to just banking institutions. It now presents itself in capital markets.

"...the Hockin Report's central recommendation is that Canada needs a single securities regulator with a strong, decentralized structure that recognizes Canada's unique make-up and regional and local expertise."

The Office of the Superintendent of Financial Institutions, which is the primary regulator and supervisor of federally-registered deposit-taking institutions, insurance companies and federally-registered pension plans, published a press release in April of 2008 which indicated that the Office of the Superintendent of Financial Institutions did not oversee the firms that created a non-bank ABCP, so these firms were not subject to its published capital guidelines. These guidelines did not apply to the offshore banks that negotiated the bulk of the liquidity lines non-bank ABCP conduits; they were subject to the capital rules of their home countries.

Citing the fact that the federal government needs to have a strong presence in the regulation of Canada's capital markets, the Hockin Report's central recommendation is that Canada needs a single securities regulator with a strong, decentralized structure that recognizes Canada's unique make-up and regional and local expertise.

The report also recommended the establishment of an independent adjudicative tribunal dealing only in securities and capital market issues.

Finally, the report recommended the regulation of exchanged traded derivatives be prescribed in securities legislation. In addition, for over-the-counter derivatives, the report recommended that the newly formed Canadian Securities Commission have sufficient policy depth and resources to determine the best path for the regulation of over-the-counter derivatives in the future.

On January 28, 2009 the federal government introduced a proposed national securities regulator as part of its budget.

After almost 18 months, the ABCP restructuring has finally been completed, albeit with minimal assistance from the federal government and three provincial governments. Nonetheless, the restructuring appears to have been completed successfully.

The report of the investment dealers highlights the significance of the releases which form part of the restructuring package and recommends sweeping changes and the method, process and procedure used by investment dealers when dealing with these esoteric financial instruments.

Finally, there is a significant movement to have Canada create a National Securities Regulator to put forward one Canadian regulated position with respect to capital markets and to have further and better controls over the derivatives market in Canada. ■

PARTNERSHIP AGREEMENTS - THEY CAN SAVE YOU HEARTACHE

John Polyzogopoulos

Disputes among shareholders in small, closely-held businesses that are often family-run are much like family law disputes. The main difference is that the battle over custody of the children is substituted for the battle for custody or control of the business. Emotions in both types of cases can run high.

When economic times are tough, the incidence of breakdown of partnerships, including marriages, can be expected to increase. Given the current economic climate, it would not be surprising if the amount of litigation arising out of such disputes were to rise.

COMMERCIAL LITIGATION UPDATE

"Although shareholder disputes have many things in common with family law disputes...the law relating to each kind of dispute is very different."

John Polyzogopoulos provides counsel in a variety of matters including shareholder disputes, breach of contract, tort claims, product liability, professional negligence, debt and security enforcement claims, insolvency and family law, particularly where the division of assets and valuation of businesses is involved. John is a member of The Advocates' Society, the Ontario Bar Association and the Toronto Lawyers' Association. He is a current board member and past president of the Hellenic Canadian Lawyers' Association.

John may be reached directly at 416.593.2953 or jpolyzogopoulos@blaney.com

For clients who may happen to find themselves in business partnerships that are no longer working for them, here are some thoughts that would be helpful to keep in mind.

Although shareholder disputes have many things in common with family law disputes in terms of the emotions involved and the lengths to which the parties will go to protect their interests (or inflict harm on the other side's interests), the law relating to each kind of dispute is very different.

Certainly, the likelihood of ending up in court over the breakdown of a relationship increases where, in the case of a marriage, there is no pre-nuptial agreement (called marriage contract in Ontario), or, in the corporate context, no pre-existing shareholders' agreement.

The absence of a shareholders' agreement, however, is much more difficult to overcome than the absence of a marriage contract. This is because, in family law, one spouse or the other is entitled by law to end the relationship unilaterally. In conjunction with that right, the principle of no-fault is very much embedded in family law, where the spouses have economic rights and obligations based on net worth and income, irrespective of their conduct. Except where the conduct of one parent can be detrimental to the best interests of the child, conduct also plays little role in determining custody, which is awarded generally to the primary care-giving parent.

When it comes to shareholder disputes, however, absent a shareholders' agreement, there is no legal right for one shareholder to remove another from the corporation or to allow a shareholder who wishes to exit the corporation to force the remaining shareholder to buy out his or her interest. There is no mechanism for an orderly division or wind-up of a corporation when one shareholder unilaterally decides that he or she wants out. Rather, as will be seen, the relevant statutory provisions focus on the parties' conduct, which, of necessity, becomes the centre of attention in such cases.

Court orders that require one party to buy out the other, or that force the liquidation or wind up of a corporation, can only be obtained in exceptional circumstances, and only following an intensive examination of the party's conduct, their interests and the best interests of the corporation. Such claims are usually made under what is known as the "oppression remedy" contained in section 248 of the Ontario *Business Corporations Act*.

In order for a complainant, usually a shareholder but often a director or creditor, to be entitled to a remedy under that section, the complainant must show that the actions (*ie.* conduct) of the corporation or any of its directors are being, or are being threatened to be exercised in a manner that is "oppressive" or "unfairly prejudicial to" the complainant, or that "unfairly disregards the interests" of the complainant. If that is the case, the court, essentially, may make "any interim or final order it thinks fit." This includes requiring the corporation to purchase a shareholder's shares, obliging one party to buy another party out, or liquidating or winding up the corporation. The focus of the section is on conduct, and only conduct.

The oppression remedy is among the broadest and most powerful remedies known in law. It is almost without precedent in any other area of the law. What can be classified as "oppressive", "unfairly prejudicial" or "unfairly disregarding

interests" is limited only by the imagination. The powers of the court are specifically limitless.

Members of Blaney McMurtry's business law group have extensive experience in advising clients on organizing their business affairs in such ways as to minimize the likelihood or impact of future shareholder disputes. This involves preparing a carefully drafted shareholders' agreement that provides for the parties' rights and obligations, including unilateral rights of dissolution. Such rights of dissolution can include rights of first refusal, shotgun rights and put or call rights, all of which have their relative advantages and disadvantages and can be tailor-made to the particular circumstances of each client.

If matters have already turned for the worse and it is too late to implement or amend a shareholders' agreement, members of our commercial litigation group can assist in navigating the treacherous waters of shareholder litigation with a view to obtaining the best possible results. ■

SPEAKING ENGAGEMENTS

April 2-3, 2009

Geza Banfai will be a presenter at The Canadian Institute's Construction SuperConference to be held in Saskatoon, Saskatchewan. Geza will present a session on "Effectively Managing Delay Claims".

January 29-30, 2009

Geza Banfai was a Course Leader at Osgoode Hall's Professional Development CLE two-day program The Intensive Course in Construction Law, held in Toronto. Geza also presented a session on "Project Delivery Models and When to Use Them".

January 29-30, 2009

Howard Krupat was a co-presenter at a session on "Construction Disputes and How to Avoid Them", at Osgoode Hall Law School's Professional Development CLE Intensive Course in Construction Law.

January 22, 2009

Geza Banfai was a co-presenter, along with Kevin McGuiness of the Ontario Attorney General Civil Crown Law Office, at a session on "Contract Management: How to Prevent or Minimize Disputes" at Osgoode Hall's Profession Development CLE Program, The Advanced Legal and Practical Guide to Public Procurement.

Editor: Howard Krupat (416.593.2998)

We welcome your comments. Address changes, mailing instructions or requests for additional copies should be directed to Chris Jones at 416.593.7221 ext. 3030 or by email to cjones@blaney.com. Legal questions should be addressed to the specified author.

EXPECT THE BEST

Blaney McMurtry
BARRISTERS & SOLICITORS LLP

2 Queen St. East, Suite 1500
Toronto, Canada M5C 3G5
416.593.1221 TEL
416.593.5437 FAX
www.blaney.com