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Legislative Update

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INCREASING CORPORATE PENALTIES AND RISK MANAGEMENT[1]

— Frank Palmay[2] and Jeffrey Nagashima,[3] McMillan LLP.

Introduction[4]

During the recent global financial crisis and the ensuing recession, governments deployed large fiscal packages to stimulate their economies, leading to dramatic increases in public indebtedness. In the U.S. and U.K. alone, governments sank US$7 trillion into financial institutions.[5] Governments are now faced with paying down the debt incurred during the crisis in addition to challenges from an uneven economic recovery and obstacles such as aging populations or declining commodity prices. As such, governments have turned to new and innovative methods to raise funds, including prosecuting civil actions more frequently than ever before, levying larger and more frequent fines for corporate malfeasance, and creating incentive programs for corporate whistleblowers.[6]

Directors and officers should think critically about their business's operations to ensure that they have not committed, and are not about to commit, any 'corporate sins.' Insurance companies should audit the operations of the large companies they insure with a view to these 'corporate sins,' and corporate counsel should remain vigilant about potential risks, ensuring that risks, especially those related to the 'seven sins' enumerated below, are elevated to the highest level of decision-making within the business.

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[1] This paper is an update to "seven corporate sins as a source of government revenue and economic stimulus" by Frank Palmay and Candice Chan-Glasgow (April 2013), available at http://www.mcmillan.ca/seven-corporate-sins-as-a-source-of-government-revenue-and-economic-stimulus.

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[4] This article has been edited significantly for length. For the full version of this article, please see http://mcmillan.ca/Files/180673_Increasing%20Corporate%20Penalties.pdf.

[5] Augusto Lopez-Claros, "Policy Research Working Paper 6805 – Fiscal Challenges after the Global Financial Crisis – A Survey of Key Issues" The World Bank Development Economics Global Indicators Group (March 2014), available at http://www-wds.worldbank.org/external/default/WDSContentServer/WDSP/IB/2014/03/17/000158349_20140317155632/Rendered/PDF/WPS6805.pdf.

[6] Gary S Lincenberg and Ariel A Neuman, "United States: white-collar criminal defence" GIR Insight (September 2014), available at http://globalinvestigationsreview.com/insight/chapter/7/united-states-white-collar-criminal-defence.

Rising Regulatory Aggressiveness

Since the financial crisis of 2009, there has been a clear trend towards larger fines for corporate malfeasance. As can be seen from the below sample of major fines in the U.S., since 2012, U.S. regulators have been able to levy over $10 billion of fines annually from only five cases a year.

Year	Entity	Fine
2012-2013	British Petroleum HSBC GlaxoSmithKline UBS Standard Charter	$4 billion $1.9 billion $3 billion $1.5 billion $667 million Total: $11.067 billion
2013-2014	JP Morgan Johnson and Johnson Deutsche Bank SAC Capital Royal Bank of Scotland	$13 billion $2.2 billion $1.9 billion $1.8 billion $610 million[7] Total: $19.51 billion
2014-2015	Bank of America Toyota BNP Paribas Credit Suisse Alstom S.A.	$16.65 billion $1.2 billion $8.9 billion $2.6 billion $772 million Total: $30.122 billion

Furthermore, governments have taken proactive steps to support increasing regulatory aggressiveness by enacting tougher legislation on white collar crime and awarding broader investigatory and penalty powers to regulatory agencies. For example, the U.K. enacted its own version of the *Foreign Corrupt Practices Act* ("FCPA"), the *UK Bribery Act*, and the U.S. enacted the *Foreign Account Tax Compliance Act* ("FATCA") to grant the Internal Revenue Service ("IRS") broader investigatory powers in pursuing tax evaders.

Evidence of the U.S. government's aggressiveness can be seen by how the U.S. deployed the *False Claims Act* in 2014 to recover an all-time record of $5.69 billion (and an aggregate recovery since 2009 of $22.75 billion),[8] the lifting of the three year hiring freeze at the U.S. Attorney's Office in 2014,[9] and comments by the chairwoman of the United States Securities and Exchange Commission ("SEC") in 2013 that certain defendants will no longer be allowed to settle actions without admitting or denying wrongdoing. Additionally, U.S. regulatory agencies are employing increasingly more aggressive tactics in their investigations, which were previously reserved for pursuing organized crime and sophisticated narcotics cases. For example, the investigation into senior Petro-Tiger executives for FCPA violations led to the general counsel wearing a wire to record future conversations.[10]

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[7] Please note that this fine was split between U.S. and UK regulators.

[8] Office of Public Affairs, "Justice Department Recovers Nearly $6 Billion from False Claims Act Cases in Fiscal Year 2014", Department of Justice (November 20, 2014), available at http://www.justice.gov/opa/pr/justice-department-recovers-nearly-6-billion-false-claims-act-cases-fiscal-year-2014.

[9] *Supra*, note 6.

[10] John F. Savarese, "White Collar and Regulatory Enforcement: What to Expect in 2015" Harvard Law School Forum on Corporate Governance and Financial Regulation (February 5, 2015), available at http://corpgov.law.harvard.edu/2015/02/05/white-collar-and-regulatory-enforcement-what-to-expect-in-2015/.

Lastly, as corporations become increasingly global, regulators have begun to cooperate on an international scale. The LIBOR scandal prompted regulators to work together to investigate the depth of the benchmark manipulation. This led to the discovery of manipulation of other benchmark rates including foreign exchange rates. Another area where regulators are working together is in cross-border tax enforcement. This has been facilitated by the recent U.S. enactment of the FATCA.

Overall, it has become apparent that there is a clear trend towards increasing regulatory aggressiveness and larger penalties for violations of 'corporate sins.'

The Seven Sins and Their Associated Regulatory Penalties

Below are descriptions of recent regulatory penalties levied against corporations.[11] These recent penalties have been arranged according to each 'corporate sin' to give the reader a sense of the magnitude and aggressiveness with which regulators will pursue organizations for each 'corporate sin.'

Sin #1: Corruption and Bribery

There has been a number of high profile cases recently where companies accused of corruption or bribery were fined by regulatory agencies. The largest penalties for corruption and bribery have been imposed by the United States government, but other governments, such as Canada, have also levied large fines for corruption and bribery. From 2002 to 2014, the United States Department of Justice ("DOJ") and the SEC imposed some $4.4 billion in fines related to FCPA violations.

Sins #2 and #3: Money-Laundering & Sanctions-Breaking

Two other corporate sins in the news are money-laundering and sanctions-breaking. A few financial settlements in the area, such as those of BNP Paribas, HSBC Holdings and HSBC Bank USA, and ING Bank N.V., total over $10 billion in penalties and forfeitures.

Sin #4: Conspiracy

Two major global scandals have occurred recently regarding conspiracies to rate fix that have implicated a number of multi-national banks and generated billions for governments worldwide through fines.

The well-publicized London Interbank Offered Rate ("LIBOR") scandal involved banks manipulating the LIBOR rate from 2005 through 2009 to profit from trades or to appear more creditworthy. Rigging the rates affected millions of consumers and the amount of interest they paid during this time. Fines assessed totalled several billion dollars.

Following the LIBOR scandal, another scandal came to light involving many of the same major banks as the LIBOR scandal. The banks were caught colluding from 2008 to 2013 to manipulate exchange rates. As a result of this scandal, regulators hit six major banks with fines totaling approximately $4.3 billion. Interestingly, five of the banks received a 30% discount on their fines by regulators for settling early. Additionally, the U.S. Office of the Comptroller of the Currency ordered the same five banks to pay an extra $1.48 billion and the Swiss regulator FINMA ordered UBS to pay $139 million.

[11] For fuller details and specific examples, please see the complete article at http://mcmillan.ca/Files/180673_Increasing%20Corporate%20Penalties.pdf.

Sin #5: Tax Evasion

Tax evasion has become a government priority lately, particularly for the IRS, which is focused on offshore tax evasion. A recent example includes Credit Suisse's guilty plea in relation to conspiracy to aid and assist U.S. taxpayers in filing false income tax returns and other documents with the IRS.[12]

Sin #6: Misuse of client property

This 'corporate sin' relates to the handling of unclaimed property. Misuse of client property keeps assets from the government and prevents governments from being able to disburse the assets back to its citizens. States, federal agencies, and other organizations in the United States are holding over $58 billion in unclaimed property. Of that total, about $41.7 billion is being held by various states.[13] Where the money is not claimed by the entitled beneficiaries, it acts a source of revenue for the state. For example, unclaimed property is Delaware's third largest source of revenue. Between 2009 and 2012, Delaware raised $1.24 billion in revenue from unclaimed property.[14]

Sin #7: Mistreatment of Customers

The seventh and final corporate sin relates to the mistreatment of customers by various financial, insurance, and automotive corporations. Consequently, these corporations have been forced to pay billions in fines to regulators and consumer class actions. Overall, the relief to borrowers and direct payments to government bodies from lawsuits over mortgages, foreclosures, and fire-sale deals totals almost $127 billion.[15]

Recent issues with auto manufacturers have been widely publicized, with a $1.2 billion fine imposed on Toyota Motor Corporation by the DOJ, and a $35 million fine imposed on General Motors Co. by the NHTSA over how it handled the recall of 2.59 million small cars.[16] Additionally, Honda Motor Co. agreed to pay $70 million in fines for failing to tell the U.S. government about warranty claims and more than 1,700 injuries and deaths linked to potential defects in its cars.[17]

Most recently, Volkswagen has been in the news for allegedly falsifying diesel emission tests. It remains to be seen how this situation will unfold and whether this will result in any multibillion dollar fines or settlement.

What Counsel Can Do

In light of increasing regulatory aggressiveness worldwide, corporations must enhance their current risk management programs. Companies need to be pro-active in dealing with 'corporate sins' and focus on prevention and detection of violations. Once a company is charged, complying with an investigation can become a huge burden. For example, Wal-Mart's internal inquiry into FCPA violations cost $439 million over two years (2013-2014)[18] and Avon's internal

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[12] Office of Public Affairs, "Credit Suisse Pleads Guilty to Conspiracy to Aid and Assist U.S. Taxpayers in Filing False Returns", Department of Justice, available at http://www.justice.gov/opa/pr/credit-suisse-pleads-guilty-conspiracy-aid-and-assist-us-taxpayers-filing-false-returns.

[13] Melanie Hicken, "$58 Billion Unclaimed: Is Some of it Yours?" CNN Money (27 January 2013), available at http://money.cnn.com/2013/01/24/pf/unclaimed-money/.

[14] Vipal Monga, "Unclaimed? Delaware Gets It" The Wall Street Journal (29 January 2013), available at http://www.wsj.com/articles/SB10001424127887323644904578269910666010352.

[15] Christina Rexrode and Andrew Grossman, "*Record Bank of America Settlement Latest in Government Crusade*" The Wall Street Journal (August 21, 2014).

[16] Jeff Plungis and Tim Higgins, "GM to Pay Record $35 Million Fine Over Handling of Recall", BloombergBusiness (May 16, 2014), available at http://www.bloomberg.com/news/articles/2014-05-16/gm-said-to-agree-to-u-s-fine-over-ignition-switch-recall.

[17] Jeff Plungis, "Honda Fined Record $70 Million for Underreporting Injuries", Bloomberg Business (January 8, 2015), available at http://www.bloomberg.com/news/articles/2015-01-08/honda-fined-record-70-million-for-underreporting-injury-claims.

[18] David Voreacos and Renee Dudley, "Wal-Mart Says Bribe Probe Cost $439 Million in Two Years", Bloomberg Business (March 26, 2014), available at http://www.bloomberg.com/news/articles/2014-03-26/wal-mart-says-bribery-probe-cost-439-million-in-past-two-years.

FCPA inquiry cost $339.7 million over four years (2009-2012).[19] To prevent charges, companies should develop an effective risk management program. An effective risk management program is composed of two parts: (1) a strong compliance program, and (2) a strong 'tone from the top.'

A strong compliance program is key to the prevention of 'corporate sin' charges. In the event of charges, the "existence and effectiveness of [a] corporation's pre-existing compliance program" is one of nine factors that the DOJ considers in determining whether to charge a corporation for an FCPA violation and what penalty to impose.[20] Key factors in an effective compliance program are: (1) written policies, procedures and guidelines, (2) training and education, and (3) effective oversight with quick responses to detected offenses. The last point requires that companies create oversight positions, such as a chief compliance officer, and that personnel in these positions be given meaningful authority. Furthermore, it is important that companies continue to upgrade their compliance programs to respond to changing circumstances.

In Canada, one pivotal sentencing decision for violations of the CFPOA[21] is *R v. Griffiths Energy International*.[22] This case summarizes a number of mitigating factors the courts will consider when deciding penalties under the CFPOA. In *Griffiths*, the company paid a bribe of $2 million to a corporate entity owned by the wife of a foreign ambassador. Of importance is the court's statement that "Griffiths has instituted an effective, comprehensive and robust anti-corruption program such that it is unlikely that there will be any repetition of such conduct[23] … These are very significant mitigating factors."[24] Therefore, it appears that one mitigating factor the Canadian courts will take into account when determining sentencing in a white-collar criminal case is an effective compliance program.

The tone from the top refers to the expectations created by management and the board regarding compliance. Part of setting the tone requires that both management and the board adhere to the same written policies, procedures and guidelines as the other employees of the corporation. Furthermore, management and the board should be required to have compliance training and education. This will show employees that management holds itself to the same standards it holds the employees. Lastly, principled performance should be rewarded. Ethical employees should be rewarded for honest behavior and reporting compliance violations.[25]

Lastly, it is important to remember that directors and officers may be held personally liable. In many of the previous examples directors and officers were charged with civil and criminal penalties. For that reason it is important that directors and officers be provided with insurance and an indemnification agreement. Directors and officers insurance protect directors and officers acting in the scope of their managerial duties against the consequences of actual or alleged wrongful acts. However, it is important to remember that these policies contain exclusion policies for fraudulent, criminal or intentional non-compliant acts.

The foregoing provides only an overview and does not constitute legal advice. Readers are cautioned against making any decisions based on this material alone. Rather, specific legal advice should be obtained.

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[19] Jaclyn Jaeger, "Analysis: The Rising Costs of FCPA Investigations" Compliance Week (March 4, 2013), available at https://www.complianceweek.com/blogs/enforcement-action/analysis-the-rising-costs-of-fcpa-investigations#.VPXnQeHDR5k.

[20] Criminal Division of the U.S. Department of Justice and the Enforcement Division of the U.S. Securities and Exchange Commission, "FCPA – A Resource Guide to the U.S. Foreign Corrupt Practices Act" Department of Justice, Securities Exchange Commission (November 14, 2012), available at http://www.justice.gov/criminal/fraud/fcpa/guidance/guide.pdf at page 62.

[21] *Corruption of Foreign Public Officials Act*, SC 1998, c. 34.

[22] *R v. Griffiths Energy International*, [2013] AJ No 412.

[23] *Supra*, note 22, at 19.

[24] *Ibid*, at 21.

[25] "Tone at the top: The first ingredient in a world-class ethics and compliance program" Deloitte (2014), available at http://www2.deloitte.com/content/dam/Deloitte/us/Documents/risk/us-aers-tone-at-the-top-sept-2014.pdf.

LEGISLATIVE UPDATE

British Columbia

Franchises

On October 20, 2015, Bill 38, the *Franchises Act* (the "FA"), received third reading. The FA, among other things:

- applies, where the business operated or to be operated by a franchisee under the franchise agreement is wholly or partly in British Columbia, to:
  - (a) a franchise agreement entered into on or after the coming into force of section 2; and
  - (b) a renewal or extension, entered into on or after the coming into force of section 2, of a franchise agreement that was entered into before, on, or after the coming into force of section 2;
- does not apply to specified relationships;
- defines several terms, including franchise, franchisor's associate, franchisor's broker, material change, material fact, and prospective franchisee;
- provides that every franchise agreement imposes on the parties a duty of fair dealing in the performance and enforcement of the agreement, including the exercise of a right under the agreement;
- provides that the duty of fair dealing includes the duty to act in good faith and in accordance with reasonable commercial standards;
- sets out provisions regarding the right of franchisees to associate;
- mandates that a franchisor must provide to a prospective franchisee a disclosure document that the franchisee must have received at least 14 days before the earlier of:
  - (a) the signing by the franchisee of the franchise agreement or other agreement relating to the franchise; and
  - (b) the payment by or on behalf of the prospective franchisee to the franchisor or franchisor's associate of any consideration relating to the franchise;
- sets out provisions regarding the delivery and content of the disclosure document;
- mandates the provision of a written statement of any material change, and sets out requirements regarding the timing of receipt thereof;
- details situations where the disclosure obligations do not apply;
- provides a franchisee with a right of rescission without penalty or obligation in specific circumstances;
- sets out the obligations of the franchisor or franchisor's associate after a rescission;
- provides that if a franchisee suffers a loss because of a misrepresentation in a disclosure document or statement of material change, or as a result of a franchisor's failure to comply with section 5 (which relates to disclosures), the franchisee has a right of action for damages against the franchisor, the franchisor's broker, the franchisor's associate, and every person who signed the disclosure statement or statement of material change (the "Document");
- provides that, subject to section 8(1), where a Document contains a misrepresentation, a franchisee who acquired a franchise to which the Document relates is deemed to have relied on the misrepresentation;
- provides that, subject to section 8(1), where a franchisor failed to comply with section 5 with respect to a statement of material change, a franchisee who acquired the franchise to which the material change relates is deemed to have relied on the information in the disclosure document;
- sets out exceptions and defences to liability;

- provides that a Document complies with section 5 despite a defect in form, a technical irregularity, or error (the "Defect") if the Defect does not affect the substance of the Document and the Document is substantially in compliance with the FA;
- provides that any purported waiver or release by a franchise or prospective franchisee of rights conferred by the FA or obligations imposed on the franchisor or franchisor's associate is void (although this does not apply to a waiver or release made in accordance with a settlement of an action, claim, or dispute); and
- provides for the making of regulations.

Certain sections of the FA also apply to a franchise agreement entered into before section 2 comes into force, and the FA comes into force by regulation of the Lieutenant Governor in Counsel.

Manitoba

Court Rules

On October 8, 2015, Man. Reg. 165/2015 (the "Regulation"), which amends *The Court of Queen's Bench Rules*, Man. Reg. 553/88, was registered. Among other things, the Regulation replaces the existing Rule 73 with a new Rule 73, *Payment Into and Out of Court*.

The Regulation comes into force on January 1, 2016.

Accessibility

On October 19, 2015, Man. Reg. 171/2015, *Customer Service Standard Regulation* (the "Regulation") under *The Accessibility for Manitobans Act*, CCSM, c. A1.7, was registered.

Among other things, the Regulation:

- explains that accessible customer service is provided when all persons who are reasonably expected to seek to obtain, use, or benefit from a good or service have the same opportunity to obtain, use, or benefit from the good or service;
- sets out timelines by which specified types of organizations are subject to sections 4 to 15 of the Regulation;
- requires organizations to establish and implement measures, policies, and practices regarding barrier-free access to the goods or services they provide, and to comply with same;
- sets out provisions regarding assistive devices, support persons, service animals, and an organization's built environment;
- mandates that organizations use reasonable efforts to ensure that, in their measures, policies, and practices, they provide a reasonable process for feedback;
- requires specified organizations to document certain information, provide notice that such documentation is available on request, and provide a copy of same on request;
- describes the obligations organizations have in respect of training about accessible customer service, and the maintenance of documentation in respect thereof; and
- sets out obligations regarding the accessibility of public events.

The regulation came into force on November 1, 2015.

Ontario

Personal Property Security

On December 31, 2015, sections 3(2), 5, and 6 of Schedule E of the *Ministry of Government Services Consumer Protection and Service Modernization Act, 2006*, SO 2006, c. 34 (the "Act"), come into force.

These sections amend the *Personal Property Security Act* by replacing section 7(3) (which relates to the location of the debtor) and by including transitional provisions in respect of sections 7 and 7.1.

Under the new section 7(3), the location of the debtor is as set out in the chart below.

No.	Debtor	Location
1.	Individual	Jurisdiction of location of principal residence
2.	Partnership (other than a limited partnership), and the governing partnership agreement states that the agreement is governed by the laws of a province or territory of Canada (a "P or T")	That P or T
3.	Corporation, limited partnership, or organization that is incorporated, continued, amalgamated, or otherwise organized under a law of a P or T that requires the incorporation, continuance, amalgamation, or organization to be disclosed in a public record	That P or T
4.	Corporation incorporated, continued, or amalgamated under a law of Canada that requires the incorporation, continuation, or amalgamation to be disclosed in a public record	Jurisdiction of registered office or head office as set out in the special Act, letters patent, articles, or constating instrument under which the debtor was incorporated, continued, or amalgamated **OR** If the above does not apply, in the jurisdiction where the registered office or head office of the debtor is located as set out in the by-laws
5.	Registered organization (as defined in the Act) organized under the law of a US state	That US state
6.	Registered organization organized under the law of the USA	If the law designates a US state of location, then that US state **OR** If the law of the USA authorizes the organization to designate its US state of location, then such designated state **OR** If the above do not apply, the District of Columbia in the USA
7.	Trustee acting for a trust	If the trust instrument governing the trust states that it is governed by the laws of a P or T, that P or T **OR** If the above does not apply, the jurisdiction in which the administration of the trust by the trustees is principally carried out
8.	Other	Jurisdiction where the chief executive office is located

Quebec

Funeral Operations

On October 22, 2015, Bill 66, the *Funeral Operations Act* (the "Bill"), received first reading. The Bill, which repeals the *Non-Catholic Cemeteries Act*, CQLR, c. C-17, and the *Burial Act*, CQLR, c. I-11, and amends certain other statutes, applies to the provision of funeral services, embalming, the interment, disinterment, and transportation of bodies, the operation of funeral facilities, the disposal of human ashes, and the disposal of unclaimed bodies. Among other things, the Bill:

- sets out funeral operations to which it does not apply;
- sets out licensing requirements;
- provides for the suspension, revocation, and refusal to renew licences;
- creates specific provisions in respect of different aspects of funeral operations (such as embalming, the operation of a cemetery, burial, cremation, etc.);
- provides for inspections and investigations; and
- contains provisions regarding contraventions of the Bill.

The Bill would come into force on the date or dates set by the government.

Saskatchewan

Farm Security

On October 20, 2015, Bill 187, *The Saskatchewan Farm Security Amendment Act, 2015* (the "SFSAA"), received first reading. The SFSAA would amend *The Saskatchewan Farm Security Act*, SS 1988-89, c. S-17.1, by, among other things:

- replacing, amending, repealing, or adding several definitions;
- repealing or replacing certain sections;
- increasing the maximum amount of certain fines; and
- adding a provision regarding administrative penalties.

The SFSAA would come into force on proclamation.

RECENT CASES

Lien Bond Did Not Satisfy Contractor's Trust Obligations Under *Builders' Liens Act*

Supreme Court of Canada, September 18, 2015

The appellant general contractor, Stuart Olson Dominion Construction Ltd. ("Stuart"), subcontracted work on a construction project to the respondent, Structal Heavy Steel ("Structal"). Stuart alleged that there were delays attributable to Structal and withheld payment, indicating that it was using the unpaid amounts for back charges resulting from the alleged delays. Structal registered a builder's lien against the property. Stuart filed a lien bond in the full amount of the builder's lien. Structal approved the bond and vacated its lien. Subsequently, Stuart received amounts from the owner, but refused to make further payments to Structal, alleging, in part, that Structal was fully secured by the lien bond. Structal asked the owner to withhold from Stuart an amount equal to its past due invoices or face an action for violating the trust provisions of *The Builders' Liens Act* (the "BLA"). Stuart applied for a declaration that it had satisfied the BLA trust obligations. Structal sought an order that Stuart was required to make full payment of all past due invoices upon Stuart's receipt of the payments from the owner. The trial court found in favour of Stuart, concluding that Stuart's filing of the lien bond extinguished its trust obligations to Structal. The Court of Appeal overturned the trial court, concluding that the right to a statutory trust and the right to a lien were separate and distinct remedies under the BLA. Stuart appealed.

The appeal was dismissed. Section 56(1) of the BLA is unambiguous that security paid into court stands in place of the land against which the lien was registered. The registration of the lien can be ordered vacated when security is paid into court, freeing the land from the lien encumbrance, but the underlying claim remains. The trust provisions of the BLA, which are found in sections 4 to 9, create a different and more wide-reaching remedy. While the lien provisions do not impose obligations on contractors or subcontractors regarding funds received, the trust provisions provide that trust funds cannot be appropriated for other purposes until all subcontractors, and others, have been paid. Although the BLA was silent as to the interaction of the two remedies when both remedies were pursued at the same time, section 66 of the BLA, which provides for the joining of a trust claim and an action to realize a lien, contemplates that the lien and trust remedies may be pursued concurrently. Section 4(3) of the BLA, which restricts the contractor from diverting trust funds for its own use until subcontractors have been paid all amounts owing to them, also supported the conclusion that the filing of the lien had no effect on the subsistence of the statutory trust. A subcontractor has not been paid simply because a lien was filed or because security was posted in order to vacate the lien. An owner, contractor, or subcontractor who chooses to file a lien bond with the court instead of depositing the funds at issue must maintain the trust fund in addition to the bond.

Stuart Olson Dominion Construction Ltd. v. Structal Heavy Steel, 2015 CCLG ¶ 25-630

Trustee Entitled To Examine Under *Bankruptcy and Insolvency Act* Despite Separate Action Against Former Directors and Officer of Bankrupt

Ontario Superior Court of Justice, September 23, 2015

SHS Management Services Inc. ("Management") was created to acquire the home services business operated by Sears Canada Inc. The Verhoeffs were the directors of Management and Lea was an officer of Management (the Verhoeffs and Lea, together, the "Respondents"). In late 2013, PricewaterhouseCoopers Inc. (the "Trustee") was appointed the interim receiver of Management and SHS Limited Partnership (together, the "Bankrupt"). In mid-2014, the Trustee was appointed in the Bankrupt's bankruptcy proceedings. In its review of the Bankrupt's records to identify and evaluate transactions that may be subject to review under, among other legislation, the *Bankruptcy and Insolvency Act* ("BIA"), the Trustee sought to examine the Respondents pursuant to section 163(1) of the BIA. Under that section, a trustee has broad powers of examination in order to collect information relevant to the Trustee's duties in administering a bankrupt's estate. The Respondents initially asked for a delay of the examinations and subsequently failed to attend examinations scheduled for March 2015. After investigation into some 2013 dividend payments to, among others, family trusts beneficially owned by the Respondents (the "Dividend Transaction"), the Trustee concluded that a cause of action likely existed. In February 2015, having been unable to reach a tolling agreement to avoid limitation issues, the Trustee commenced an action (the "Action") against the Respondents with respect to the Dividend Transaction. The Trustee brought a motion seeking an order compelling the Respondents to attend examinations and deliver specified documents, pursuant to section 163(1). The Respondents argued that the Trustee, having commenced the Action, was not entitled to examine them pursuant to section 163(1), absent exceptional circumstances. The Respondents took the position that the information sought by the Trustee would be available through discovery in the Action and the Trustee should not be able to use section 163(1) of the BIA as a "dress rehearsal" for the Action.

The motion was granted. Competing interests might arise between a trustee's right to examine to facilitate administering a bankrupt's estate and avoiding the use of that power to promote litigation. However, in this situation, imposing a requirement of "exceptional circumstances" to permit a section 163(1) examination was too high. The more appropriate test was for the Court to be assured that the examination was necessary for the due administration of the Bankrupt's estate and was not a "mere step in the action." The Trustee's proposed examination under section 163(1) of the BIA was necessary for due administration of the Bankrupt's estate. The Respondents were directly involved with the Bankrupt. The Trustee had sought to hold the examination well before commencing the Action. Commencement of the Action was necessary as the parties had been unable to reach a tolling agreement to deal with the limitation period. The Trustee's proposed examination dealt with many issues beyond the Dividend Transaction that was the subject of the Action. The implied undertaking rule ensured that any information obtained in the Action could not be used in the bankruptcy, and the Court directed that the portion of the section 163(1) examination dealing with issues in the Action apply as discoveries in the Action so as to avoid repetition.

SHS Services (Re), 2015 CCLG ¶ 25-631

Court Dismisses Appeal of Summary Judgment

Ontario Court of Appeal, September 18, 2015

The trustee in bankruptcy (the "Trustee") had obtained access to funds totalling almost $1 million. The appellant, Mirkais Investments Inc. ("Mirkais"), was owned by the spouse of the bankrupt and was the assignee of a 1992 General Security Agreement ("GSA") that the bankrupt had granted to a bank. Mirkais claimed to be a secured creditor entitled to the funds obtained by the Trustee and challenged the Trustee's disallowance of its claim for the funds. Mirkais subsequently sued its lawyer, the respondent, for negligence for failing to appeal the disallowance as instructed. The motion judge dismissed Mirkais's argument that some of the funds received by the Trustee were secured collateral under the GSA, noting, among other things, that neither the bankrupt nor his spouse gave evidence that the bankrupt had any interest in or right to the collateral. Accordingly, they had no prior perfected security interest in the funds under the *Personal Property Security Act* ("PPSA") that would defeat the Trustee's right to the funds. Section 11(2) of the PPSA requires the debtor to have rights in the collateral in order for the security interest to attach; section 19 provides that only security interests that are "attached" can be perfected; and section 20(1)(*b*) requires that the security interest over the collateral be perfected in order to take priority over the Trustee's interest. The motion judge granted the lawyer's motion for summary judgment on the basis that, without an enforceable security interest, Mirkais was unable to prove damages, a necessary element in a negligence action. Mirkais appealed, making the additional argument that, but for the lawyer's alleged negligence, Mirkais would not have lost the chance to prove the secured claim and the value of the lost chance could underpin a negligence claim.

The appeal was dismissed. Mirkais had not shown that the motion judge made a legal error or a palpable and overriding error of fact, and there was no new evidence that the bankrupt had any interest in the funds at issue. As to the "loss of chance" argument, which was an accepted basis for proving damages in support of negligence, Mirkais's failure to invoke the "lost chance" principle in its claim, or advance it before the motion judge, precluded it from seeking relief on this new basis. In addition, both the bankrupt and his spouse, who was the principal of Mirkais, had maintained that the bankrupt had no assets of any kind. It was "inconceivable" that Mirkais could have taken a position in the bankruptcy that was so at odds with the sworn evidence of its principal. There was no evidence that Mirkais had lost the chance of an advantage of some real, substantial monetary value.

Mirkais Investments Inc. v. Klotz, 2015 CCLG ¶ 25-632

Author Fails To Establish Primary or Secondary Copyright Infringement

Ontario Superior Court of Justice, September 18, 2015

The plaintiff, Miguna, was the author of a book about his life in Kenya (the "Book"), which was published in 2012 under a publishing agreement with Gilgamesh Africa Ltd. (although there was some dispute about this). In August 2014, Miguna became aware that the Book was offered for sale on the walmart.com website and was advertised on the website as being published by the defendant Consortium Book Sales and Distribution, LLC ("Consortium"). Consortium's website identified the publisher as Gilgamesh Publishing Ltd. ("Gilgamesh UK"). The Court noted that even "the plaintiff did not, until comparatively recently, at least in this action, distinguish between Gilgamesh UK and Gilgamesh Africa ...". The walmart.com website was controlled by an affiliate of Wal-Mart Stores Inc. Consortium and Wal-Mart Stores Inc. were based in the United States and the websites were operated from there. Miguna claimed that he did not consent to any publication, production, reproduction, or release of the Book by the defendants and commenced a claim for copyright infringement. The *Copyright Act* (the "Act") distinguishes between primary and secondary infringement. Miguna acknowledged that he was alleging primary infringement only against Consortium, and secondary infringement against Consortium and Wal-Mart Stores Inc. Under section 27(2) of the Act, secondary infringement occurs when any person, among other activities, sells, distributes, or offers for sale a copy of a work that the person knew or should have known infringed copyright. The defendants argued that Miguna could not satisfy the test for secondary infringement under the Act because there was no evidence of primary infringement of the Book. The defendants further argued that even if infringing copies of the Book existed, they never dealt with the Book, never received copies of it, and never possessed the Book in any form. The defendants also pointed to the territorial principle, noting that there had to be a sufficient connection to Canada for the Act to apply. The defendants brought motions for summary judgment to dismiss the action.

The motions were granted. The test for summary judgment was that there be no genuine issue for trial (see *Hryniak v. Mauldin*, 2014 SCC 7). The test for secondary infringement was: (a) there must be a primary infringement; (b) the secondary infringer should have known that he or she was dealing with a product of infringement; and (c) the secondary infringement sold, distributed, or exposed for sale the infringing goods (*Euro Excellence Inc. v. Kraft Canada Inc.*, 2007 SCC 37). There was ample evidence on which to conclude that none of the moving parties had ever physically received or sold a copy of the Book in North America, let alone Canada. Further, there was no evidence that the defendants dealt with any copy of the Book not produced by Gilgamesh Africa Ltd. Although the walmart.com website could be seen by Canadian Internet users, items on the website could not be purchased by persons in Canada or shipped to addresses in Canada. The mere ability to view the website was not sufficient to create a meaningful nexus to Canada and engage the remedies provided under the Act. The Court found that the most plausible explanation as to why Consortium was represented as the publisher of the Book was an error by the distributor. Miguna failed to discharge his evidentiary burden to establish primary copyright infringement on a balance of probabilities. Without primary infringement, there was no basis for Miguna's claim of secondary infringement, and there was no basis for the claim of infringement of Miguna's moral rights. The defendants therefore satisfied the requirement to establish that there was no genuine issue for trial.

Miguna v. Walmart Canada, 2015 CCLG ¶ 25-633

Alberta Appropriate Venue for Multi-Jurisdictional Class Proceeding

Court of Queen's Bench of Alberta, September 30, 2015

Kohler and Cooke filed a proposed negligence class action in Alberta in September 2013 against the defendant drug manufacturers, claiming that the mispackaging of oral contraceptives led to unwanted pregnancies and other damages. The proposed national class included all women in Canada who took the specific oral contraceptive between August 2012 and June 2013 and the biological fathers of individuals born to these women between specified dates. The intervenors commenced a proceeding in Ontario in November 2014 on behalf of a similar prospective national class (the "Kutlu Action") with comparable claims against the same defendants. The Kutlu Action expressly including subrogated claims, including on behalf of Ontario's provincial health plan. The Kutlu Action was not yet certified as a class action in Ontario. The plaintiffs applied to certify their action as a class action under the *Class Proceedings Act* ("CPA"). The proposed representative plaintiffs in the Kutlu Action received intervenor status at the certification hearing and made written submissions advocating deference to the Ontario proceeding because the Kutlu Action expressly dealt with subrogated claims. In light of their submissions, the plaintiffs amended their claim to include subrogated interests. At the hearing, the Court considered whether it should certify the action as a multi-jurisdictional action or grant deference to the Ontario proceeding. Under section 9.1(1)(*b*) of the CPA, certification of a multi-jurisdictional proceeding requires a court to determine under section 5(6) that Alberta is the appropriate venue. In order to make that determination, consideration of the objectives set out in sections 5(7)(*a*)–(*d*) is required (meeting the interests of all parties, serving the ends of justice, avoiding irreconcilable judgments if possible, and promoting judicial economy). Section 5(8) of the CPA provides that, "[w]hen making a determination under subsection (6), the Court may consider any matter that the Court considers relevant but must consider at least the following": the alleged basis of liability, including applicable laws, the stage each proceeding has reached, the plan for the proposed proceeding, the location of class members, representative plaintiffs, evidence, and witnesses, and the advantages and disadvantages of litigation in more than one jurisdiction (sections 5(8)(*a*)–(*f*) of the CPA). The intervenors took the position that deference should be granted to the Kutlu Action, arguing, among other things, that they had signed up more class members with potentially more serious claims.

The action was certified as a multi-jurisdictional class proceeding with a national class. Consideration of the following objectives under section 5(7) of the CPA yielded a neutral outcome with respect to whether Ontario or Alberta was the appropriate venue: meeting the interests of all parties, serving the ends of justice, and promoting judicial economy. Only Alberta had a legislated mandate under section 5(7)(*c*) of the CPA to avoid irreconcilable judgments if possible, but deference by Alberta courts in all cases to jurisdictions without such a legislated mandate would significantly impede prospective class proceedings in Alberta. Accordingly, while this factor was appropriately taken into account, it could not be the sole determining consideration. Considering the six factors under section 5(8), five of the six factors did not necessarily weigh in favour of either Alberta or Ontario. Consideration of the section 5(8)(*b*) factor (the stage of each proceeding), however, clearly weighed in Alberta's favour as Alberta's action was significantly ahead of the Ontario proceeding. Alberta's action was now certified as a class action, while the only step toward certification in Ontario was a meeting date to discuss a schedule for a potential certification application (whether the meeting had occurred was unknown to the Court). Courts have been slow to stay a class proceeding before them where a parallel proceeding in another jurisdiction has not yet been certified, especially if potential class members would not be adequately protected. The potential to be included in a separate out-of-province action at some unknown time was no reason to preclude the plaintiffs from pursuing their properly filed ongoing action in Alberta. Certifying a multi-jurisdictional class proceeding did not require the plaintiffs in the Kutlu Action to abandon it. They were free to opt out of the Alberta proceedings and advance other actions.

Kohler v. Apotex Inc., 2015 CCLG ¶ 25-634

Board Erred in Failing To Consider All Potential Uses of Word Marks, Not Just Actual Use

Federal Court, September 16, 2015

One of the applicants was a winery that produced and bottled wine in association with the marks PINNACLES and PINNACLES RANCHES; another applicant winery used the mark PINNACLE under a licence agreement. The PINNACLES mark had been used in Canada since 1993. The respondent, Domaines Pinnacle Inc., applied to register DOMAINE PINNACLE & DESIGN (the "Word and Design Mark") in association with its apple-based alcoholic beverages and apple-based non-alcoholic products. The design depicted an apple overlaid with a snowflake. The applicants opposed Domaines Pinnacle Inc.'s application before the Trade-marks Opposition Board (the "Board") on several grounds, and particularly on the basis of confusion. The Board applied the test for confusion under section 6(2) of the *Trade-marks Act*, considered each of the factors under section 6(5), and rejected the opposition. The Board concluded that while there was a fair degree of resemblance between the particular marks, visually speaking, the marks suggested different ideas. The apple element in the Word and Design Mark suggested the idea of apple-based products, and the snowflake element suggested the idea of cold and winter. By contrast, the mark PINNACLES of the applicants suggested the idea of a plurality of summits. The Board also noted that there was an absence of confusion between the trademarks amidst coexistence in the Canadian marketplace. The Board ruled that there was no reasonable likelihood of confusion between the applicants' marks and the respondent's Word and Design Mark. The applicants appealed the Board's decision and argued that the Court should consider the matter *de novo*.

The appeal was granted, the decision of the Board was set aside, and the matter was remitted for reconsideration. A *de novo* consideration was not appropriate. The new evidence submitted by the applicants was not of sufficiently probative value that it would have materially changed the Board's analysis and its decision. Applying the standard of review of reasonableness, the Board erred in its determination of the degree of resemblance between the marks. That error impacted the Board's "global analysis" of the factors under the confusion test. Because a registered word mark can be presented in many ways under the registration, when applying the confusion analysis to a registered word mark, all the potential uses permitted by a registration, not just the actual use, must be considered. The Board's analysis of the degree of resemblance between the two marks hinged on the visual element and the ideas suggested. The Board should have taken into account that the mark PINNACLE could have a different presentation, with changes in the style of lettering, colour, or design. Those differences could have suggested the "idea of cold and winter", similar to the applied-for Word and Design Mark. The Board erred in failing to consider the registered word mark according to its terms rather than its actual use.

Constellation Brands Inc. v. Domaines Pinnacle Inc., 2015 CCLG ¶ 25-635

Terms of Bank's Agreement Constituted Complete Defence to Claim for Reimbursement for Forged Cheques

Supreme Court of British Columbia, September 11, 2015

The plaintiff, D2 Contracting Ltd. ("D2"), opened a business bank account (the "Account") with the defendant, The Bank of Nova Scotia (the "Bank"), in January 2006. D2's two owners, Cooper and Copeman, were joint authorized signors on the Account, and Copeman maintained the Account and received monthly statements. Although the Bank could not locate the original Account documents, when the Account was opened, the Bank's standard form of documentation included a Financial Services Agreement (the "Agreement"). The Agreement dealt with, among other provisions, the cheque clearing system used by the Bank. Under paragraph seven of the Agreement, the Account holder was responsible for verifying the Account and had 30 days after the mailing of the statement to notify the Bank of errors, after which there was no claim against the Bank. Paragraph 13 of the Agreement limited the Bank's liability for the Account holder's loss in connection with the Bank's services, and specifically noted it had no liability for "forged, unauthorized or fraudulent use of services ... even if you or we did not verify the signature, instruction or authorization" (instruction was defined in the Agreement to include cheques). Cheques on the Account required two signatures. In April 2009, Cooper informed the Bank that Copeman had allegedly forged Cooper's signature on a number of cheques. D2 claimed that, between March 2006 and April 2009, Copeman had forged 594 cheques. In an undefended hearing, Copeman was found liable for fraud and D2 obtained a judgment of $1,289,600. D2 then commenced action against the Bank for the return of the funds it alleged were wrongfully withdrawn from the Account. The Bank argued, among other things, that D2's claim was completely answered by its failure to follow the verification requirements in the Agreement, and that, apart from contractual defences, Cooper had actual knowledge of Copeman's forgeries and failed to provide the Bank with timely notice. D2 argued, among other things, that the Bank had breached section 48 of the *Bills of Exchange Act* (the "Act") by honouring the forged cheques, and that the limitation of liability in the Agreement was unenforceable because of ambiguity. The Bank applied for summary trial to dismiss the claim.

The application was granted and D2's action was dismissed. Having regard to the totality of the circumstances, proceeding by way of summary trial was a fair process to achieve a just adjudication of the issues. On a balance of probabilities, and despite being unable to locate the signed Agreement, the Bank proved that the parties had entered into the Agreement: it accorded with sound commercial practices that the Account could not have been opened without Cooper and Copeman having signed a number of standard form documents. The Bank was not obliged to bring specific terms of the Agreement, including the payment clearing provisions, to the attention of Cooper and Copeman. Cooper's allegation that he did not know that the authenticity of the signatures on the cheques would not be verified in the cheque clearing process unless the cheque was negotiated at the home branch of the Bank was not a basis for finding that the Agreement was unenforceable: failure to read a contract before signing it is not determinative of whether a business person is bound by its terms. Section 48 of the Act was not a strict liability provision. Under that section, the Bank had no liability for honouring a forged cheque since D2 was precluded from recovery in this instance as a result of the liability limitations in the Agreement. Even applying a strict construction against the Bank, the wording of the Agreement as a whole was not ambiguous. Paragraphs 7 and 13 of the Agreement imposed on the Account holder the obligation to review and verify the statements and report errors within 30 days. The Bank's liability for forgeries after the 30-day period was clearly limited even if the Bank did not verify the signature. The evidence established that Cooper took no steps for almost three years to inform the Bank of the forgeries. He had received a compensation cheque as early as 2006 that did not bear his signature and yet did not inform the Bank. Cooper further acknowledged that in 2009, Copeman had signed payroll cheques in his absence and Cooper did not make an issue of his signature having been forged on such cheques. In any event, and under the circumstances, the Agreement provided a complete defence to D2's claims.

D2 Contracting Ltd. v. The Bank of Nova Scotia, 2015 CCLG ¶ 25-636

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