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**Threats and Opportunities:  
Litigating Under OBCA/CBCA**

**Monday, May 1, 2006**

Ontario Bar Association  
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Monday, May 1, 2006

9:00 a.m. to 5:00 p.m.

OBA Conference Centre, 200-20 Toronto Street, Toronto

Chair: **Markus Koehnen**, McMillan Binch Mendelsohn LLP

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**Dissent and Appraisal Rights: A Right With No Remedy?**

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# DISSENT AND APPRAISAL RIGHTS: A RIGHT WITH NO REMEDY?

Tom Curry and Usman Sheikh\*

*Lenczner Slaght*

The enactment of the dissent and appraisal rights in Canadian corporate law was well intentioned. The relevant statutes, that is, attempted to strike a balance between, on the one hand, the interests of a majority who sought to institute fundamental structural changes to a corporation and, on the other, the rights of a minority that refused to participate in changes that radically altered the nature of the corporation beyond what they had initially contemplated. In striking this balance, the *CBCA* (s. 190) and *OBCA* (s. 185) (collectively, the “Acts”) provide frameworks that grant shareholders, who dissented from specified corporate acts, a statutory right to demand that the corporation purchase their shares for “fair value.” As the Dickerson Committee noted, “[t]he result is a resolution of the problem that protects minority shareholders from discrimination and at the same time preserves flexibility within the enterprise.”<sup>1</sup>

## I – Impediments to Recovery

Since its very inception, however, these rights have been the subject of intense criticism due to major impediments involved in recovering under the right. Involving a litany of notices, counter-notices and deadlines, such rights have often resulted in protracted proceedings before the court requiring a judge to engage in the arduous task of fixing the fair value for the shares. Accordingly, and as early as 1962, Professor Bayless Manning, one of the leading American critics, questioned the value of such a right in light of, what he considered to be, a slow, laborious, and expensive procedure that generated unpredictable awards. Summing up his concerns, he had this to say:

It appears to be reserved to lawyers to understand that a remedy without a procedure for obtaining it, is not worth very much... If the appraisal remedy entails substantial cost – indeed, even modest cost – or if the holders are required to hang in uncertainty for a protracted period, the game of appraisal is usually not worth the candle. The usefulness of the remedy depends on the ease and efficiency of the procedure...<sup>2</sup>

These concerns over the efficacy of the dissent and appraisal procedure were echoed in Canada as recently as in the costs judgment of *Ford Motor Co. of Canada v. Ontario Municipal Employees Retirement Board*, [2005] O.J. No. 1377 (S.C.J.), aff’d, [2006] O.J. No. 990 (C.A.), leave to appeal filed, [2006] S.C.C.A. No. 77 (S.C.C.) (“*Ford Motor F*”). Noting the practical realities facing shareholders in order to recover from a corporation under the right, Cumming J. lamented:

From a practical standpoint, it is impossible for virtually any minority shareholder to effectively challenge a corporation’s statutory offer because the costs of a court proceeding are prohibitive. It is only the institutional shareholder that can even consider mounting a

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<sup>1</sup> R. W. V. Dickerson, J. L. Howard & L. Getz, *Proposals for a New Business Corporation Law for Canada* vol. 1 (Ottawa: Information Canada, 1971) at p. 115.

<sup>2</sup> B. Manning, “The Shareholder’s Appraisal Remedy: An Essay for Frank Coker,” (1962) 72 *Yale L.J.* 223 at p. 230.

meaningful challenge. Even if successful in obtaining a higher value, and receiving costs on a partial indemnity basis, the minority shareholder would perhaps suffer a net loss because of the net costs to be absorbed. Most corporations can be comfortable in their view that virtually all minority shareholders will take the statutory offer made rather than fight it with attendant non-reimbursable costs and accompanying opportunity costs in waiting for their money. Indeed, the corporation may discount its offer in the first instance because of the knowledge of the cost to dissenting shareholders of a challenge. (Q.L., para. 57)

Given the above concerns, this paper briefly reviews some of the factors to consider in deciding whether to exercise the dissent right and pursue an appraisal hearing under the *Acts* and, in so choosing, offers methods to do so in a cost-effective and efficient manner.

## II – Considerations: Before Commencing Litigation

Before commencing a court proceeding to determine the fair value of shares, a shareholder and corporation should consider the following sobering question: Is it really worth it? In addition to the significant time requirements and efforts that both parties must expend in following the labyrinthine provisions of the *Acts* and, ultimately, engaging in litigation, the following factors should also be considered:

(i) Unpredictable Awards: Valuations by the court in order to determine, what Farley J. once referred to as, the “etherial concept of fair value”<sup>3</sup> for shares, are by their very nature inherently unpredictable. Although the courts have recognized several valuation techniques in order to arrive at such a determination,<sup>4</sup> fixing fair value remains, at the end of the day, a question of judgment by the court. As Lambert J.A. of the British Columbia Court of Appeal stated in *Re Cyprus Mining Corp. and Dickson et al.* (1986), 33 D.L.R. (4<sup>th</sup>) 641 (B.C.C.A.):

... the problem of finding fair value of stock is a special problem in every particular instance. It defies being reduced to a set of rules for selecting a method of valuation, or to a formula or equation which will produce an answer with the illusion of mathematical certainty. Each case must be examined on its own facts, and each presents its own difficulties.... The one true rule is to consider all the evidence that might be helpful, and to consider the particular factors in the particular case, and to exercise the best judgment that can be brought to bear on all the evidence and all the factors. I emphasize: it is a question of judgment. No apology need be offered for that. Parliament has decreed that fair value be determined by the courts and not by a formula that can be stated in the legislation. (Q.L., p. 8)

The unpredictability of determining fair value is no more evident than in the following recent cases where the parties, themselves, advanced widely divergent positions: *Enterprise Payment Solutions Inc. v. Soft Tracks Enterprises Ltd.*, [2005] B.C.J. No. 847 (B.C.S.C.) (shareholders claimed \$172,500 for shares; corporation valued shares at \$1); *Ford Motor Co. of Canada, Ltd. v. Ontario Municipal Employees Retirement Board*, [2004] O.J. No. 191 (S.C.J.), varied, [2006] O.J. No. 27 (C.A.) (“*Ford Motor IP*”) (shareholders claimed \$642.50 per share; corporation offered to settle initially at \$150 per share, subsequent offer at \$265).

<sup>3</sup> *New Quebec Raglan Mines Ltd. v. Blok-Andersen*, [1993] O.J. No. 727 (Ont. Gen. Div.) at p.1 (Q.L.).

<sup>4</sup> In *Brant Investments Ltd. v. KeepRight Inc.*, [1991] O.J. No. 683 (C.A.), the Ontario Court of Appeal identified four accepted approaches to the valuation of shares: the market value approach, the asset value approach, the earnings approach and some combination of the preceding three approaches (Q.L., p. 31).

(ii) Expenses: Expenses for appraisal hearings, moreover, can quickly and easily become considerable. In addition to incurring the expenses normally associated with litigation (which can include the costs of documentary production, cross-examining on affidavits, conducting examinations for discovery, interviewing witnesses, motions, attendance at hearings, and other counsel fees and disbursements), parties in appraisal proceedings have been particularly burdened with the requirement of retaining eminent valuation experts to support their position on fair value and generating extensive expert reports to that effect. Expert evidence is particularly important in the context of fair value hearings because courts, who technically bear the onus of fixing fair value, have nevertheless imposed a legal burden on parties to advance evidence to assist the judge in arriving at that determination and have long preferred the evidence of experts (see *Andres Wines Atlantic Ltd. (Re)*, 1996 N.S.J. No. 459 (N.S.S.C.) at para. 14; see also *Enterprise, supra*). When all the dust has settled, the cost of such proceedings can be staggering as is made clear from the following passage from *Ford Motor II, supra*:

The trial consisted of some 49 days of evidence in oral submissions, accompanied by comprehensive written submissions... There were several witnesses, including four expert witnesses for each side, the extensive expert reports and voluminous documentary evidence of some 22 banker's boxes with 132 Exhibits and 49 volumes of joint books of documents... All experts are eminently qualified in their respective areas of expertise.... [Furthermore, the] great complexity of the extensive transactional and economic data under analysis, and of the many issues at play, led to ongoing revised expert evidence and reports throughout the trial. (Q.L., paras. 1-2)<sup>5</sup>

(iii) Uncertainty on Recovering Costs: Parties should also consider the uncertainties associated with recovering the costs of litigation following a fair value hearing. While, as noted by Dennis Peterson, a trend has emerged to “award costs against the corporation where all else is equal,”<sup>6</sup> this is not always so. Albeit a unique case, the court in *Ford Motor I, supra*, awarded the dissenting shareholders their costs on a substantial indemnity basis up to the date of the corporation’s first offer to purchase the dissenter’s shares yet found the corporation to be entitled to its costs, on a partial indemnity basis, from that point forward. A court will also divide costs in cases where success on a determination of fair value was divided, and have awarded costs against shareholders where they caused substantial delay, declined offers to settle which were higher than the amount ultimately fixed by the court, failed to produce adequate evidence to support their position and were substantially unsuccessful in convincing the court of the amount for fair value which they claimed.<sup>7</sup>

(iv) Taxable Event and Brokerage Costs (Shareholders): As Professor MacIntosh notes, election of the appraisal option by a dissenting shareholder may also trigger the burden of a taxable

<sup>5</sup> The precise costs for this particular proceeding are unknown as the trial judge held that if the parties could not agree on the quantum of costs, the matter was to be assessed by an assessment officer (*Ford Motor II, supra*, at para. 60).

<sup>6</sup> D. Peterson, *Shareholder Remedies in Canada* (looseleaf) (Toronto: Butterworths, 2006) at p. 15.31. See, for example, *Nunachiaq Inc. v. Chow*, [1993] B.C.J. No. 3003 (B.C.S.C.) Parties should also consider the consequences of Rule 49 (“Offer to Settle”) of the Ontario *Rules of Civil Procedure*.

<sup>7</sup> See, for example, *Smeenk v. Dexeigh Corp.*, [1990] O.J. No. 1500 (H.C.J.), aff’d, [1993] O.J. No. 2020 (C.A.).

event for that shareholder.<sup>8</sup> Moreover, to the extent that the shareholder decides to reinvest, the reinvestment of funds will also result in brokerage costs that would not have been incurred had the investment continued in the enterprise.<sup>9</sup>

(v) The Message (Corporations): In the face of a significant and growing number of dissenters, a corporation may also wish to reconsider the benefit of the proposed fundamental change before engaging in fair value proceedings. As several commentators note, the use of the last-resort mechanism of the dissent right by a substantial number of dissenting shareholders who feel the decision was so improvident that the market no longer offers a fair alternative, should exert a salutary effect upon management by forcing the corporation to reconsider whether the transaction is, in fact, value-increasing.<sup>10</sup>

### III – Considerations: Commencing Litigation

After engaging in a cost-benefit analysis with the above considerations in mind and deciding to apply to the court for a determination of fair value, there are several ways, at the outset of the litigation, to reduce costs and ensure the efficient disposition of a fair value hearing:

(a) Making and Accepting a True Fair Value Offer: In the first instance, corporations should be encouraged to make realistic and “true” fair value offers and dissenting shareholders should refrain from making unreasonable demands. Recent case law has made it easier for corporations to make such offers. As the Court of Appeal held in *Ford Motor Company of Canada, Ltd. v. Ontario Municipal Employees Retirement Board*, [1997] O.J. No. 4298 (C.A.) (“*Ford Motor III*”), except in the unusual circumstance where an admission is made in a pleading (as in *Roytor & Co. v. Skye Resources Ltd.*, [1986] O.J. No. 25 (H.C.J.), aff’d, [1986] O.J. No. 1342 (C.A.)), a statutorily required fair value offer will not be considered an admission as to the minimum fair value of the shares permitting a dissenting shareholder to move for partial summary judgment. Rather, “[t]he rules should be interpreted so that corporations are encouraged to make a true fair value offer, not an offer premised on the corporation’s view as to the minimum value that might be set after the prolonged and complex litigation that [such] applications appear to engender.” (Q.L., p.14) To the extent that parties decide to make unreasonable offers and dissenting shareholders decide to make exorbitant demands, the courts have often made such parties face the cost consequences of their actions. As the court stated in *Smeenk v. Dexeigh Corp, supra*, it is “appropriate and fair to use the ‘carrot and stick approach’... to achieve reasonableness on the part of the company in making its offer which ought to be its best; and to achieve reasonableness in the expectations of the shareholder in deciding whether to accept the company's offer. Neither the company nor the shareholder ought to expect a “free ride” in the court if they do not agree. In my opinion, the party

<sup>8</sup> See J. MacIntosh, “The Shareholders’ Appraisal Right in Canada: A Critical Reappraisal,” (1986) 24 *Osgoode Hall L. J.* 201 at pp. 249-254.

<sup>9</sup> *Ibid.*, pp. 254-255.

<sup>10</sup> *Ibid.*, p. 265; F. Iacobucci, M. Pilkington, R. Prichard, *Canadian Business Corporations: An Analysis of Recent Legislative Developments* (Agincourt: Canada Law Book, 1977) at p. 171.

who is seen to be unreasonable ought to pay for intransigence by having to assume some or all of the financial burden of the proceedings” (Q.L., p. 46).

(b) Application vs. Action: Parties initiating fair value hearings should also turn their mind to the nature and suitability of the originating process. The *Acts* specifically provide for a corporation (or, failing which, the shareholder) to initiate an appraisal hearing by way of application.<sup>11</sup> By exploiting the cost-effective and streamlined procedures inherent in such proceedings, such applications provide a summary procedure for the fixing of a fair value of a dissenter’s shareholding particularly in non-complex matters. There are several advantages, however, to determining fair value by commencing an action. From the perspective of the corporation, it may be better to proceed by way of action because of the access to cross-examine witnesses that is available to the dissenting shareholder in the procedures that govern applications. As Hugh DesBrisay notes, “on an application, the dissenting shareholder will have the right to subpoena witnesses on the pending application and will have rights to cross-examine officers and directors of the corporation, the corporation’s auditors and the expert valuers retained by the dissenting shareholders (among others). In contrast, rights of discovery in an action are restricted to an examination of one representative of the corporation.”<sup>12</sup> At times, moreover, proceeding by application is simply not practical in light of the complexity of the matter. The court in *Anthem Works*, [2005] B.C.J. No. 1226 (B.C.S.C.) decided to convert the matter to an action in light of questions surrounding the *bona fides* of the dissenter’s conduct; the complex questions raised by the proceedings; the complicated question of determining the appropriate methodology of valuation; the benefit that pleadings would provide to frame the issues in the case; and the courts belief that the “tried and true” procedures under the *Rules of Court* would lead to a more timely and orderly resolution of the dispute. (Q.L., para. 72)

(c) Venue: When it is apparent that shareholders will reject a corporation’s initial offer to purchase their shares or the corporation opts to produce no such offer,<sup>13</sup> a corporation would be well-advised to initiate fair value proceedings in the district where it has its head office in order to avoid dealing with appraisal proceedings in multiple jurisdictions. As the court held in *Persona Communications Inc. v. Mahoney*, [2004] O.J. No. 5180 (S.C.J.), corporations have the first opportunity to commence such proceedings and to choose the venue<sup>14</sup> and, once chosen, *forum conveniens* principles need not be considered (Q.L., para. 17-18). Failing to initiate proceedings, however, can result in applications being made by dissenting shareholders in other districts, or even other provinces, forcing a corporation to incur significant and unnecessary costs before all such actions are joined.

<sup>11</sup> See CBCA, s. 190(15) & (16) and OBCA, s. 185(18) & (19).

<sup>12</sup> H. DesBrisay, “Dissent Proceedings: Update on Procedural and Substantive Issues,” *Corporate Litigation Update* (Toronto: Dept. of Continuing Legal Education, Law Society of Upper Canada, 1999) at p. 2.

<sup>13</sup> See CBCA, s. 190(12)-(15) and OBCA, s. 185(15)-(18).

<sup>14</sup> Subject to statutory restrictions. See CBCA, s. (17).

#### IV – Considerations: During Litigation

Finally, during the course of the litigation, parties to an appraisal hearing ought to consider the following tips in order to ensure that their money is well spent and to avoid unnecessary or wasted costs:

(a) Experts: While the courts have stated on several occasions that they will not be bound by the opinion of experts, their judgments as to the fair value of shares have long been guided, and have often turned, on the findings contained within such reports. By considering factors that courts have used to give greater weight to some reports over others, the following are helpful suggestions to ensure that this (often necessary) expense does not go to waste.

(i) *Timeliness of the Report*: Courts have often given added weight to expert opinions prepared closer to the valuation date or to the moment in time when the events in issue occurred (see, for example, *Re Brant Investments Ltd. et al. and KeepRite Inc. et al.*, [1987] O.J. No. 574 (H.C.J.) at p. 29). With respect to “timeliness,” while the dissenting shareholder in *Xerox Canada Inc. v. Ontario Municipal Employees Retirement System (OMERS)*, [1991] O.J. No. 1154 (Ont. Gen. Div.) conceded that a report conducted over a year and a half after the corporation’s initial offer was of less value, the court, nevertheless, concluded that it would still be of some value for the dissenting shareholder to prepare an expert report in that case. (Q.L., p. 6)

(ii) *Management Consultations and Interviews*: The court in *Fraser Inc. v. Aitken*, [1988] O.J. No. 1962 (H.C.J.) also indicated that it would prefer reports prepared by experts who had direct consultations and interviews with persons responsible for the management of the corporation to reports prepared on the basis of transcripts of evidence given by such individuals at an examination for discovery. Such consultations, moreover, should be informal interviews where a valuator could obtain “franker and more spontaneous disclosure” (Q.L., p.11).

(iii) *Industry Consultation*: The court in *Fraser, supra*, also gave added weight to the report of an expert who had discussions with and prepared his report on the basis of information given by professionals who were not affiliated with the corporation yet were knowledgeable about the relevant industry of the corporation. It may not be sufficient, the court noted, for an expert to rely upon general literature regarding an industry in order to form an opinion (Q.L., p.11).

(b) Obtaining Information: With the intention of providing dissenting shareholders an opportunity to produce an expert report that satisfies the requirements of section IV(a) above, the courts have recognized the availability, in certain cases, of a unique form of “pre-discovery” in which the dissenter’s valuator is given an opportunity to interview management at the corporation in advance of normal discovery obligations provided in the *Rules of Civil Procedure* for actions or applications (see *Xerox, supra*). While such “pre-discovery” proceedings have the potential to become extremely lengthy, time consuming and the subject of motions, counsel can minimize this eventuality by (on the corporation’s part) volunteering those documents and witnesses that would likely be relevant to the shareholder’s valuator (as was done in *Ford Motor Co. of Canada Ltd. v. Ontario Municipal Employees Retirement Board*, [1999] O.J. No. 1263 (Ont. Gen.Div.) (“*Ford Motor IV*”)) and by (on the shareholder’s part) requesting only those documents and witnesses that are necessary to produce an expert report comparable to that of the corporation’s.

Both sides of the litigation should be guided by the principles in *Xerox, supra*, which adopted a “balanced approach” in order to give the valuator “as good an opportunity as possible, while at the same time protecting the individuals and intruding on the affairs of [the corporation] as little as possible.” (Q.L., p. 8). Applying this balanced approach, the court ordered only that which was necessary and included additional safeguards: in that case, the President of Xerox Canada was to be interviewed; the interview was to take place in the President’s office so as to “provide conditions as close to ‘normal’ as possible;” to the extent that commercially sensitive information was to be divulged, a confidentiality undertaking (or agreement) was to be given; the interview was to be conducted by the shareholder’s expert with counsel taking no part except to object to the substance or form of a question; and, finally, in light of the oppression remedy aspect of the suit, the interview was to be recorded and conducted in the presence of counsel (Q.L., p. 7).

## V – Conclusion

*Ex ante*, it may not be clear whether the appraisal right will result in a benefit or a major burden to an individual shareholder or corporation. This paper, however, has attempted to outline some factors that parties ought to consider in order to determine whether to exercise the right and, further, whether to request a court to fix the all-elusive fair value of its shares. It has also attempted to outline cost-effective and efficient measures to consider when commencing and proceeding with an appraisal hearing with the goal of working with provisions in the *Acts* that have long been considered as providing a right with no remedy.