SUPREME COURT OF NOVA SCOTIA
Citation: *Big X Holdings Inc. v. Royal Bank of Canada*, 2014 NSSC 368

Date: 20141014
Docket: Hfx No. 406111
Registry: Halifax

Between:

Big X Holdings Inc., Robert Leonard McNeil, and Margaret Anne McNeil

Plaintiffs

v.

Royal Bank of Canada

Defendant

DECISION

Judge:	The Honourable Justice Gerald R. P. Moir
Heard:	September 9, 2014, in Halifax, Nova Scotia
Counsel:	Mark Bailey, for the Plaintiffs D. Geoffrey Machum, Q.C. and Colin Piercey, for the Defendant

Moir J.:

Introduction

[1] The plaintiffs lost a lot of money they invested in a company. The defendant financed the investment, and it later became the company's banker. The plaintiffs say that the defendant is responsible for their losses because it breached implied terms of banking or lending contracts, or it breached fiduciary obligations, requiring the defendant to supervise the company.

[2] The plaintiffs elected trial by jury. The defendant moves for trial without a jury.

Apparent Facts

[3] According to financial statements, "The Advance Commission Company of Canada provides commission advances to real estate agents." It recorded revenue "when the deal is approved and money is advanced to the client", which suggests it took some kind of assignment of the commission due on agreement of purchase and sale and realized revenue through some portion of the commission given up by the agent. Legitimate financial statements suggest the return was substantial.

[4] The sources of cash for these "advances" were shareholder investments and bank financing. Mr. and Ms. McNeil, and their holding company, became investors in early 2007. They bought shares and made shareholder loans. There was another passive investor, and the president, Gregory Burden, was also a shareholder.

[5] The Royal Bank financed the plaintiffs' investment in Advance Commission, but it also took over as banker for the company a few months after the initial investment by the McNeils and their holding company. That happened in May and June, 2007.

[6] The money lent to the plaintiffs consisted in a $600M line of credit for Big X, a $250M term loan to it, and personal lines of credit to the McNeils totalling $330M. Various guarantees, pledges, and mortgages were given to secure these loans.

[7] Lending agreements and securities were amended in 2009 and 2011. As a result, the operating line was $500M, the term loan was $55,000, and a new term loan stood at $240,000. Apparently, the personal lines continued.

[8] When the Royal Bank became Advance Commission's banker in May and June of 2007, it provided the company with an operating line of credit capped at

the lesser of $8m or 75% of accounts receivable limited to $100,000 per agent and $250,000 per broker. The overall limit was increased to $10m in 2010, then $15m in 2011.

[9] The bank took security over all property of the company. It also took limited guarantees from the president and the other shareholders.

[10] The Advance Commission company agreed to deliver to the bank monthly certificates about compliance with the borrowing limits, monthly internal financial statements, and audited annual statements.

[11] Mr. Burden is not a party to this proceeding. He provided no evidence on the present motion, and he was not given an opportunity to challenge the evidence that was presented. What follows is my interpretation of the evidence provided by the bank. Blunt words are required, but they are used with knowledge that Mr. Burden is not bound.

[12] Each year for a number of years, Mr. Burden forged financial statements of Advance Commission. He took auditor-prepared (review engagement) financial statements and altered the statements of income and retained earnings and the balance sheet to overstate income, retained earnings, and shareholder equity. A big part of the deception was a massive overstatement of accounts receivable,

$18,475,251 as of September 30, 2011 according to the fraudulent statements and $12,043,683 according to the real statements.

[13] One assumes the fraud extended to, and was reconcilable with, the internally prepared monthly statements and the monthly certificates delivered by Mr. Burden to the bank. One assumes that these statements were given to the other investors.

[14] The evidence on the motion suggests that Mr. Burden acted alone. No one else knew about the fraud. Not other employees, not the other investors, and no one at the bank.

[15] Despite the requirement for audited financial statements, the bank accepted review engagement statements each year from 2007 to 2010. When the limit was raised, the bank insisted on audits. Audited financial statements were due ninety days after Advance Commission's September 30, 2011 year-end.

[16] It seems that only a slip of the pen brought the fraud to light. In April of 2012, Mr. Burden delivered a document titled "Grant Thornton Non-Consolidated Financial Statements The Advance Commission Company of Canada Limited September 30, 2012".

[17] On inquiry by the bank, Mr. Burden delivered new statements bearing the same title but with the date changed to September 30, 2011. In both instances, the

auditor's report was the same. Over the signature of Grant Thornton appears "We have audited the accompanying non-consolidated financial statements …".

[18] Mr. Burden had also delivered a copy of the curious 2012 report to Mr. McNeil. Noticing the reference to 2012, Mr. McNeil contacted the accountant at Grant Thornton responsible for Advance Commission. Grant Thornton sent copies of the real statements. They were unaudited and contained a review engagement report, rather than an auditor's report.

[19] As I indicated, the forged balance sheet overstated accounts receivable by $6,431,568. The forged statement of retained earnings showed $7,831,056 compared with $1,499,488. The forged balance sheet had shareholder's equity at $7,931,076 compared with $1,599,508. The main focus of the fraud was the accounts receivable, which governed most of the bank's lending to Advance Commission.

[20] Mr. McNeil immediately warned the bank, and he confronted Mr. Burden. Mr. Burden wrote to Mr. McNeil, "I am very sorry for the deception over the years …".

[21] This court appointed a receiver of the Advance Commission company on motion of the Royal Bank. The bank also sued the company, Mr. Burden, and related companies.

[22] The plaintiffs had not been customers of the bank before Mr. McNeil approached one of its officers for the initial loans. By that time, the plaintiffs had decided to invest in Advance Commission. The investment decision had nothing to do with the bank.

[23] Mr. McNeil claims he relied on the bank's oversight of its accounts at Advance Commission. There were no written or oral statements supporting that concept. The plaintiffs suggest the grounds for reliance were communicated by conduct and by the general terms of executed documents.

[24] The evidence before me suggests no controversy over documentary evidence and little or no controversy in the oral testimony.

Claim

[25] The plaintiffs did not produce evidence on this motion. The statement of claim covers the factual background in detail. It says that a $400,000 guarantee purported to have been signed by Mr. McNeil is a forgery and a claim for a

declaration to that effect is sought. Otherwise, the claims for liability are all in para. 38, which reads:

> Big X, RLM and MAM state that RBC owed them a duty of care in dealing with the account of ACC, either as an implied contractual term of the contracts between them or as a fiduciary, and that RBC breached that duty or those duties in that:
>
> (a) RBC lent and continued to lend money to ACC at prime, the rate reserved for RBC's best customers, so as to lead Big X, RLM and MAM to conclude that their loans to ACC were secure;
>
> (b) RBC never advised Big X, RLM and MAM that the activity in ACC's accounts did not support the volumes of business reported in the annual statements;
>
> (c) RBC never advised Big X, RLM and MAM that the annual detailed accounts receivable list was not consistent with the business reported by ACC;
>
> (d) RBC acquiesced in the late filing of annual statements and the waiving of the requirement that same be audited, in contravention of the offer of finance, and despite concerns from RLM directed to RBC;
>
> (e) In 2011 in contravention of the offer of finance RBC allowed ACC to wait until April 2012 before filing audited statements (some 180 days after the September 30, 2011 business year end) thus contributing to the loss by that delay;
>
> (f) RBC failed to match monthly accounts receivable statements to subsequent activity in the accounts of ACC;
>
> (g) RBC failed to require ACC to provide copies of notices of assessment from Canada Revenue Agency, and failed to therefore note that approximately $2,000,000 in income taxes purportedly owed by ACC were not paid;
>
> (h) RBC failed to note that ACC had lent large amounts of money to a company owned and controlled by PB, in contravention of the offer of finance;
>
> (i) RBC failed to exercise due diligence in advancing the initial loan, and when increasing the loan amounts;
>
> (j) RBC in contravention of its own policies allowed PB at the outset to collect written guarantees from the other shareholders of ACC which allowed PB to forge same;

(k) RBC failed to recognize that the annual statements provided by ACC were forgeries, despite internal inconsistencies.

The plaintiffs also propose that conduct by the bank over the years will point to an implied term.

[26] The primary liability issues to be determined at trial are whether there was an implied term in the banking and lending contracts that the bank would exercise care to protect the plaintiffs in respect of Advance Commission, whether the bank was a fiduciary to the plaintiffs, and whether the fiduciary duties included taking care to protect the plaintiffs in respect of Advance Commission.

Jurisprudence on Jury Election

[27] The plaintiffs rely on certain passages from the decision of a seven-judge court in *Sattva Capital Corp. v. Creston Moly Corp.*, 2014 SCC 53.

[28] The British Columbia *Arbitration Act* restricted appeals from a commercial arbitrator to questions of law. The question in that case was how to interpret a contract that required payment in shares but did not make it clear what day the shares would be valued at.

[29] Justice Rothstein, who wrote for the Court, referred to the "historical approach" (see paras. 43-46) by which all interpretation was a question of law. That approach "should be abandoned" (para. 50). Also at para. 50:

> Contractual interpretation involves issues of mixed fact and law as it is an exercise in which the principles of contractual interpretation are applied to the words of the written contract, considered in light of the factual matrix.

Justice Rothstein went on to point out that mixed questions of fact and law may be so bound up with one another that there is an inextricable question of law proper to an appeal, see paras. 53 to 55.

[30] When setting the stage for these passages, which are at the heart of the Court's determination of "When is Contractual Interpretation a Question of Law?", Justice Rothstein traced the origin of the historical approach to "a time when there were frequent civil jury trials and widespread illiteracy" (para. 43). Interpretation was reserved to judges by the device of labelling all interpretation questions as questions of law.

[31] Although *Sattva Capital* does not comment on contractual interpretation by juries, the implication is as the plaintiffs urge. A question of contractual interpretation is not automatically taken from the jury.

[32] The substantive right to a civil jury has been recognized and protected in Nova Scotia for a very long time. See Justice Warner's "excellent and thorough history of the evolution of jury trials in Nova Scotia" in *Geophysical Service Inc. v. Sable Mary Seismic Inc.*, 2008 NSSC 79, affirmed 2008 NSCA 83, leave refused [2012] S.C.C.A. 245. The appraisal is Justice Farrar's in *Anderson v. Cyr*, 2014 NSCA 51 at para. 29.

[33] There is no point in repeating what is to be found in *Geophysical* or at paras. 34 to 41 of *Anderson*. As I understand the Rules and these decisions, there is no inconsistency between what "justice requires" in the present Rules and the need for "cogent reasons" established by past jurisprudence.

[34] Courts have shown us examples of the kinds of circumstances that may, depending on the case, provide cogent reasons for trial by a judge rather than a jury. At para. 41 of *Anderson*, Justice Farrar summarized these as "the substantive issue is one of law not fact", "the issues of law and fact are so entwined with one another as to be virtually inseparable", "the case involves scientific or technical issues that cannot be conveniently presented to the jury", and "the evidence is extensive and complex."

[35] However, the discussion of past authorities at paras. 42 to 62 of *Anderson* makes it clear that, as is said at para. 43, the concept of complexity underlies all the examples. The discussion shows that factual complexity is "rarely sufficient to take away the right to a trial by jury" (para. 54), but a case dominated by questions of law (para. 52) and a case in which fact-finding and legal determinations are virtually inseparable is usually more suited to trial by judge (para. 53).

[36] These are not hard and fast examples of the kinds of complexity that will outweigh the right to trial by jury, "complexity remains a very nebulous concept" (para. 50). The question is circumstantial.

[37] *Anderson v. Cyr* provided ten "considerations to be taken into account by a motions judge in determining whether to strike a jury notice" (para. 97). The list of ten is in para. 96. Most prominent among them for the present motion is the seventh, which reads:

> If the issues of fact are difficult to isolate and are clearly interwoven with the issues of law, the motions judge must decide if the issue has risen to a level that it ought to be taken from the jury, always keeping in mind that it is a *prima facie* and substantive right that a party is entitled to have a trial by jury.

[38] There is another consideration, one that did not arise on the facts of *Anderson v. Cyr*. A sticky issue comes forward when it is proposed that a jury

became involved with a judicial discretion or an equitable claim. Justice Warner confronted that issue in *Geophysical*.

[39] Section 34 of the *Judicature Act* is the statutory foundation for the right to trial by jury in civil proceedings. It refers to trials "of a legal or equitable nature". Paragraph 34(a)(ii) provides, without reference to the distinction between law and equity, a qualified right to require "the issues of fact to be tried or the damages to be assessed or inquired of with a jury".

[40] Although s. 34(a)(ii) does not expressly restrict a jury to legal claims, the distinction between law and equity revives in s. 34(c). Legal and equitable issues raised in the same proceeding are to be heard and determined together. Exceptions are made for severance by a judge "… unless under the foregoing provisions of this Section either of the parties requires that the legal issues of fact be tried with a jury …". Note the adjective "legal" and the implication that facts going to an equitable claim are not for a jury.

[41] In *Geophysical*, Justice Warner considered the text of s. 34 in the context of the history of jury trials (paras. 41 to 57), equity as exclusively judicial (paras. 58 to 64), and the legislative history of s. 34 starting with our *Judicature Act* of 1884.

[42] Justice Warner extensively reviewed Nova Scotia case law on the right to a jury trial and the judicial power to override the right (paras. 80 to 89). He commented on the very few of those cases involving equity (paras. 90 to 101). He construed the text of s. 34(3).

> The plain meaning of subsection 34(3), is that equitable issues, including equitable issues of fact, are not for juries -- only legal issues of fact are for juries, in any proceeding where both legal and equitable issues are raised. (para. 102)

[43] Justice Warner also decided that context, especially the historical context and the common law, supported his interpretation of the plain meaning (paras. 101 and 102). In his summary of conclusions at para. 116, Justice Warner included:

> recognizing that legislation respecting court practice and procedures since merger of the courts of common law and of equity has not been as explicit in Nova Scotia as elsewhere, the application of the rules of interpretation of statutes to the *Judicature Act*, and the whole of s. 34, both grammatically and in the context of the history of the Act and the origins of the practices of the courts of common law and equity, supports the conclusion that equitable issues of law, fact and remedy are not matters properly or historically for determination by juries.

Application on this Motion

[44] The issue considered in *Sattva Capital* was "When is Contractual Interpretation a Question of Law?" What did the contract provide for a valuation date? The first question on this motion is "When is the implication of a term into a contract a question of law?"

[45] There are three kinds of cases in which a court has power to modify the literal terms of a contract by implying a term: *M.J.B. Enterprises Ltd. v. Defence Construction (1951) Ltd.*, [1999] S.C.J. 17 at para. 27. The pleadings in this case could only engage the third of these:

> the parties are presumed to intend the term because it is necessary to give business efficacy to the contract or because the situation is such that an officious bystander would say, if asked, that the parties had obviously assumed the term was part of their bargain.

[46] When lawyers give opinions about an implied term on the third basis, or judges do so in the form of a judgment, they draw on these legal skills. The call for the "necessary" or the "obvious" has to be understood in the broad context of contract law, and especially the fundamental principles about freedom of contract and certainty. The implication of a term is always going to involve expertise in law, which is our province, and expertise in finding facts, which we share with lay people.

[47] So, I agree with and follow *Collette v. Cartier Partners Securities Inc.*, 2005 BCSC 501 in which Justice Macaulay held that the implication of a term imposing a duty to exercise due diligence is "largely, if not entirely, a question of law": para. 26.

[48] The plaintiffs propose that the jury answer factual questions, such as "Did the bank's conduct point to the purported term?", "Did the plaintiffs rely on the bank to superintend the company?", and so on. A serious argument about an implied term is seldom so simple that discrete fact-finding is going to lead to the right conclusion. Questions such as the above are only part of the important facts: e.g., What do the contracts say? Which applies to whom? What motivated them? If the plaintiffs relied on the purported term, was their reliance reasonable? Why was the term not made express?

[49] Where implication of a contractual term is arguable, the determination will usually be too nuanced for a clear division of facts, extricable for the jury, and law. In this case, the court needs to determine the facts in all of their detail when determining the ultimately legal question of an implied term. In other words, the facts and the law will be too intertwined for anyone to decide the facts without an eye on the law and *vice versa*.

[50] The second and third liability issues take us to a question of law, a question of intertwined law and fact, and the distinction between law and equity.

[51] The question of whether the bank was fiduciary to the plaintiffs may involve straightforward fact-finding if the plaintiffs rely simply on the *ad hoc*

banker/customer relationship. In that case, there would likely be no factual dispute. If the plaintiffs propose something beyond the *ad hoc* fiduciary relationship, the court would have to decide whether there was a special or *per se* relationship: *Galambos v. Perez*, 2009 SCC 48.

[52] Like an arguable case for or against an implied term, a serious argument for a *per se* fiduciary relationship involves a nuanced and highly circumstantial inquiry. Law is not easily severed from fact.

[53] The content of a resulting fiduciary duty also entwines fact and law to such a degree that the questions may be inextricable.

[54] Overarching all of that, is Justice Warner's conclusion in *Geophysical*, which I follow, that fact-finding on an equitable claim is not for a jury. So, the second and third issues described at para. 26 above would have to be separated, if a jury were to undertake the impossible task of finding all the facts on the first issue, implied term.

Conclusion

[55] This is not a case for fact-finding by a jury. The complexity lies in the inextricable mixture of detailed questions of fact and the law on the main liability

issues. Also, the need for a separate determination of facts going to the equitable claim complicates the use of a jury because of the expense of separate determinations and the risk of conflicting findings of fact on implied term or fiduciary duty.

[56] Therefore, the motion is allowed. Counsel provided fine work in written and oral submissions. I thank them for that. They may send me written submissions on costs, if need be.

Moir J.