SUPREME COURT OF NOVA SCOTIA
Citation: Scanwood Canada Ltd. (Re), 2011 NSSC 495

Date: 20111219
Docket: Hfx. No. 342377
Registry: Halifax

IN THE MATTER OF: The *Bankruptcy and Insolvency Act*, R.S.C. 1985, c. B-3, as amended

AND IN THE MATTER OF: The *Judicature Act*, R.S.N.S. 1989, c. 240

AND IN THE MATTER OF: Scanwood Canada Limited (in Receivership)

DECISION

Judge: The Honourable Justice Suzanne M. Hood

Heard: December 15, 2011

Written Decision: January 20, 2012 *(Written release of oral decision of Dec. 19, 2011)*

Counsel: Stephen Kingston, Q.C. and Joseph McNally
for the Receiver
Brian Stilwell and Brett Harrison for IKEA Supply AG
Jamie MacNeil and Tracy Smith for Royal Bank of Canada
Joseph Pettigrew for the Province of Nova Scotia

By the Court:

[1] Scanwood's Receiver seeks court approval to destroy dressers produced by Scanwood which IKEA has declined to buy. Royal Bank of Canada ("RBC") opposes the destruction of the dressers. It submits that the buy-back agreement requires IKEA to purchase the dressers; alternatively, that equity requires IKEA to purchase them; or, in the further alternative, that the court should order the dressers to be sold to third parties at a liquidation sale.

[2] The issues are:

1. *Res judicata*;
2. If the matter is not barred by the doctrine of *res judicata*, does the court have authority to order IKEA to purchase the inventory, or
3. Can the dressers be sold to a third party?

FACTS

[3] The Receiver has possession of Scanwood's inventory. It consists of dressers IKEA produced for sale to IKEA. There are 8,557 so-called firsts and 2,492 seconds. The Buy-back Agreement between Scanwood and IKEA provided:

> Buyer agrees, notwithstanding sections 1.2 and 15.1 of the General Purchasing Conditions, but subject to other terms of this Agreement regarding quality of products, in the event of insolvency of, or appointment of Receiver for, the Seller, that Buyer will fulfill its obligations to acquire the products hereunder by acquiring the stock of ready made articles from the Receiver or other person in lawful control of the Seller's stock; and (ii) to the extent the Buyer does not acquire the raw materials stock of the Seller, the Receiver or other person in lawful control of the Seller's stock may (a) sell any of the IKEA fittings or products with IKEA markings only to other IKEA suppliers of the MALM product; and (b) sell any of the wood, veneers, glue, boxes and other generic product, provided that such do not contain any IKEA markings or fittings, to any person.

[4] In my previous decision of June 29, I concluded that, because of the trademark issue, the dressers could not be sold to third parties if IKEA did not buy them.

[5] IKEA has done an inspection of a portion of the inventory of firsts and agreed to buy only 675 at a reduced price. It has also agreed to buy all of the seconds. These transactions have not been concluded.

[6] The Receiver requested of IKEA that IKEA agree to have the remaining dressers donated to charity. In his email to the Receiver, counsel for IKEA said that IKEA gives tens of millions of dollars to charity each year and then said: "That being said, they indicated that they could not agree to release the remaining inventory for safety and quality issues."

Res judicata

[7] IKEA says the court has already dealt with these issues and they cannot be re-litigated.

[8] In *Danyluk v. Ainsworth Technologies Inc.*, 2001 SCC 44, the Supreme Court of Canada said at para. 18:

> The law rightly seeks a finality to litigation. To advance that objective, it requires litigants to put their best foot forward to establish the truth of their allegations when first called upon to do so. A litigant, to use the vernacular, is only entitled to one bite at the cherry. The appellant chose the ESA as her forum. She lost. An issue, once decided, should not generally be re-litigated to the benefit of the losing party and the harassment of the winner. A person should only be vexed once in the same cause. Duplicative litigation, potential inconsistent results, undue costs, and inconclusive proceedings are to be avoided.

[9] In *Angle v. M.N.R.*, [1975] 2 S.C.R. 248, the Supreme Court of Canada said at page 254:

> Lord Guest in *Carl Zeiss Stiftung v. Rayner & Keeler Ltd. (No. 2)*, at page 935, defined the requirements of issue estoppel as:
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> ...(1) that the same question has been decided; (2) that the judicial decision which is said to create the estoppel was final; and, (3) that the parties to the judicial decision or their privies were the same persons as the parties to the proceedings in which the estoppel is raised or their privies....

[10] In *Grandview v. Doering*, [1976] 2 S.C.R. 621, the Supreme Court of Canada at page 636 quoted from a Nova Scotia decision, *Fenerty v. The City of Halifax*, (1920), 50 D.L.R. 435, (N.S.S.C.) as follows:

> The doctrine of *res judicata* is founded on public policy so that there may be an end of litigation, and also to prevent the hardship to the individual of being twice vexed for the same cause. The rule which I deduce from the authorities is that a judgment between the same parties is final and conclusive, not only as to the matters dealt with, but also as to questions which the parties had an opportunity of raising. It is clear that the plaintiff must go forward in the first suit with his evidence; he will not be permitted in the event of failure to proceed with a second suit on the ground that he has additional evidence. In order to be at liberty to proceed with a second suit he must be prepared to say: "I will shew you this is a fact which entirely changes the aspect of the case, and I will shew you further that it was not, and could not by reasonable diligence have been ascertained by me before."

[11] Most recently, in 2009, the Nova Scotia Court of Appeal dealt with the issue in *Kameka v. Williams*, 2009 NSCA 107. The court in para.12 quoted the passage from *Danyluk* which I have quoted above and then said in para. 13:

> [13] Detailed statements can be found of the constituent elements necessary to establish that the doctrine of *res judicata* is applicable (see for example George Spencer Bower and Sir Alexander Turner, *The Doctrine of Res Judicata*, 2nd ed....) These were compressed by the Alberta Court of Appeal in *420093 B.C. Ltd. v. Bank of Montreal*, [1995] A.J. No. 862 where O'Leary J.A. wrote:
>
> > [18] A prior judicial decision will not raise an estoppel by *res judicata*, either issue estoppel or cause of action estoppel, unless (i) it was a final decision pronounced by a court of competent jurisdiction over the parties and the subject-matter; (ii) the decision was, or involved, a determination of the same issue or cause of action as that sought to be controverted or advanced in the present litigation; and (iii) the parties to the prior judicial proceeding or their privies are the same persons as the parties to the present action or their privies.

[12] There can be exceptions as the court found there was in *Danyluk*. In commenting on that in *Kameka*, the court said in para. 21:

> 21 The respondent did not argue cause of action estoppel, only issue estoppel. Binnie J. wrote that the rules governing issue estoppel should not be mechanically applied, in light of the underlying purpose of balancing the public interest in finality of litigation with the public interest in ensuring justice is done on the facts of a particular case. Binnie J. found that the preconditions to establishing issue estoppel had been met. The appellant nonetheless argued that the court should exercise its discretion to refuse to apply the doctrine. Binnie J. agreed that there can be no doubt that the court has such a discretion. It is to be exercised to ensure that the proper operation of issue estoppel is not at the cost of real justice in the particular case. He set out seven factors that were relevant to the exercise of the

> court's discretion in the context of an issue having been resolved in a prior earlier administrative tribunal proceeding. Binnie J. reflected that the final and most important factor was to consider if, given the entirety of the circumstances, the application of the doctrine would work an injustice. He found it would, in light of what he termed "the stubborn fact" the appellant's claim for commissions worth $300,000 had never been properly considered and adjudicated.

[13] The court then continued in para. 22:

> 22 How and if the doctrine of estoppel by *res judicata* might apply to prevent the respondent from again suing the appellant Kameka depends on whether the present suit is in relation to the same or a different cause of action.... If it is a different cause of action, consideration would have to be given to whether the party should have raised it in the earlier proceeding. However, if the suit is based on the same cause of action, it has become merged into the judgment the respondent obtained in the Small Claims Court.

[14] The court then referred to cases where it was submitted that it would be unjust to allow the doctrine of *res judicata* to prevent further litigation. In those referred to in paras. 27 and 28, the court concluded that the doctrine of *res judicata* prevented further litigation. The court, in para. 32, referred to *Gough v. Whyte*, [1983] N.S.J. No. 42 (N.S.S.C.T.D.) where Justice Grant concluded there were special circumstances. In that decision, Justice Grant said in paras. 27 and 28:

> [27] I find that to permit the plaintiff to continue would not contravene public policy. I find that to permit the defendant, in this case, to hide behind the Small Claims Court judgment would be a breach of public policy. The defendant had knowledge of the insured's claim before the Small Claims Court action was started.

> [28] I find that special circumstances exist in this case which permit the plaintiff to continue notwithstanding the judgment of the Small Claims Court.

[15] The question for me is whether the doctrine of *res judicata* applies here and, if it does, are there special circumstances which should permit the matter to be re-litigated. I refer to the three requirements of issue estoppel which I have quoted from *Angle*, *supra*.

[16] In the June 29 decision, I said in the opening para.: "In this case, the Receiver is seeking an order with respect to finished goods and raw materials of two types: some with the IKEA stamp on them and some without." I then referred to the buy-back provision and I said of it in para. 7: "It is made subject, specifically, to quality terms. In my view, this is a reasonable provision to protect IKEA." I then said in para. 8 "With respect to the finished product, IKEA agreed to purchase that finished product, if satisfied with respect to quality.

[17] The parties who participated in that matter included Mr. MacNeil for RBC and the transcript at page 57, (Exhibit "E" to Ms. Isemeyer's affidavit), shows that

he stated "... the bank does support and adopt the Receiver's submissions." The decision was not appealed and is therefore a final decision.

[18] The real issue with respect to *res judicata* is whether the same question has been decided or whether it is an issue that could have been raised. If the latter, I must be satisfied that some new evidence is before me which changes the case.

[19] The buy back provision was squarely before me on June 29th. I specifically referred to the issue of quality in para. 7. I said, with respect to the quality term and buy back agreement:

> If the company is experiencing financial difficulties which lead to insolvency or the appointment of a receiver, there is good reason for IKEA to be concerned, in particular, about quality of the product produced. Examples of the problems which could occur in a company facing financial problems are such things as a reduction in the workforce or labour strife; or an inability to purchase material which could lead to the use of substandard or defective materials on hand, to name just two examples. In such circumstances it is logical that IKEA's principal concern about buying products in these circumstances would be the quality of the product.

[20] Furthermore, the trademark issue was the paramount issue and I said in para. 9:

> 9. In my view, the more significant issue is the trademark issue. It is clear from the paragraph in the agreement to which I have just referred that IKEA was concerned about its trademark. It made specific provision with respect to materials with its trademark and a separate provision with non-trademark materials.

[21] I then said in para. 12:

> 12. If the product cannot be sold to third party because of trademark issues and IKEA does not buy it (or, in the case of some material, other suppliers of the MALM dresser), it is worthless or would be so unless the trademark can somehow be removed from it.

These are, in my view, the same issues before me now.

[22] RBC says IKEA has only raised the issue of quality now as the only means by which it can free itself of its obligations under the buy back agreement. However, as the passages above show, quality was the very issue raised by IKEA when the buy back provision was inserted in the January 21, 2011 Purchase Agreement between Scanwood and IKEA. From the affidavit material filed in this hearing, it is clear that this one time only clause was put in the agreement after negotiations with the RBC. As Ms. Isemeyer said in para. 9 of her affidavit:

> 9. In May 2010, in order to satisfy RBC's conditions to continue to support Scanwood by granting an extended line of credit, ISAG agreed to facilitate a

> "buy back arrangement." RBC proposed a "buy back arrangement" under which ISAG, among other things, would agree to buy from a Receiver all of Scanwood's outstanding finished goods inventory at 100% of invoice value. RBC also proposed that any quality restrictions for these purchases by ISAG be waived. ISAG rejected this proposal.

[23] Quality was an issue between IKEA and RBC before the CCAA proceedings were begun.

[24] The sale of dressers to third parties was at the heart of the June 29 hearing. Trademark concerns were voiced by IKEA then.

[25] In the penultimate paragraph of that decision, para. 23, I concluded:

> I have sympathy for the general body of creditors who may be unable to have the benefit of the Receiver's sale of the materials referred to in this motion. However, I cannot conclude that it is an appropriate exercise of my discretion to override IKEA's trademark. If trademarked goods are sold other than as agreed between Scanwood and IKEA, in my view, there is a serious infringement of the purpose of the trademark protection; that is, differentiating its products and the quality of products from others. There is no guarantee of the quality of these products. The second purpose of trademark protection is to allow the consumer to buy with confidence from a source they trust so they know what they are getting. In my view, this would be interfered with as well.

[26] I conclude the issues before me are the same as those in issue on June 29th. The notice of motion for the June 29 hearing stated that the Receiver was applying for an order "Providing directions to the Receiver as regards disposition of

Finished Goods Inventory and Raw Materials inventory current in the possession of the Receiver."

[27] The trademark issue has been decided. The question before me in June was whether the dressers could be sold to a third party. The issue of donating them to charity could have been raised at that time. It raises the same issues with respect to trademark as the third party sale issue.

[28] The appraisal prepared for RBC does nothing to address the trademark issue. The appraiser's intent to re-label only the boxes is inconsistent, in my view, with my decision about IKEA's trademark.

[29] As Exhibit "I" to Ms. Isemeyer's affidavit clearly shows the IKEA trademark is displayed in many places, not only on the box. It is on the instruction sheets, the fittings bag and on the metal draw slides themselves.

[30] Is there new evidence before me now which changes the case in such a way that I should conclude I should reopen the matter?

[31] RBC says there is new evidence before me, the report of an appraiser who provided an "Orderly Liquidation Values Appraisal." The five page document is Exhibit "A" to Ross Backman's affidavit. The appraiser says he has "inspected and appraised the finished Inventory." He also says: "We have taken into account the inventory might have to be re-labelled to hide the IKEA name and it is included in our reconciliation." He then concluded the inventory has a value of $322,825.00. In Exhibit "A" to his report, he lists the items valued totalling 8,557 dressers.

[32] The affidavit of Brian Stilwell attached as exhibits a series of questions and answers with respect to that appraisal. The last two questions and answers are as follows:

> Provide details of DSL inspection of the inventory, including:
>
> a. When it was completed;
> b. Who completed it;
> c. What steps were taken during the inspection
>
> We at Danbury Industrial inspected the inventory during the time we were at the site setting up for the auction sale and we opened one package to see what markings and labeling would be necessary to change. We determined the only reasonable way was to change the one on the box.

> Was DSL provided with, and did it consider, the result of IKEA's July 26, 2011 inspection in advance of preparing its Order Liquidation Appraisal dated November,
>
> NO

[33] Also attached to Mr. Backman's Affidavit as Exhibit 2 is the inspection report prepared by IKEA (which the appraiser did not have) of the 137 units that were inspected. According to Ms. Isemeyer's Affidavit in para. 29, of the 137 dressers inspected, 29 passed quality inspection and 108 failed. Based upon that inspection, IKEA agreed to purchase 675 dressers.

[34] Although not a significant number were inspected by IKEA, only one box was opened by the appraiser. Is this evidence which satisfies me that the matter should be reopened? I conclude it does not. The buy back agreement provided that IKEA would buy the dressers in the event of insolvency or appointment of a Receiver. IKEA agreed "subject to other terms of this Agreement regarding quality of products."

[35] In my view, the decision with respect to quality is a decision to be made by IKEA. Furthermore it is not at all clear from the appraiser's report that he considered the issue of quality.

[36] I therefore do not consider this new evidence to be so compelling that I should reopen the issue with respect to the buy back agreement. This is especially so, in my view, because the trademark issue referred to above is not addressed in such a way that my decision of June 29 is followed.

[37] Are there other special circumstances that cause me to exercise my discretion to grant the RBC's request in spite of the fact that these issues were previously litigated?

[38] The sale to a third party was addressed in the June hearing and in my decision. The Receiver has reluctantly made this application because he needs to give vacant possession of the Scanwood building to its new owner.

[39] RBC does not want the dressers destroyed but sold. It is certain that the other creditors would not be in favour of incurring the expense of destruction at a cost in

excess of $40,000.00. IKEA has said it does not want the dressers destroyed but says there is no other option.

[40] I, too, am reluctant to see this occur, but that was a result that could have been contemplated because of my June decision. I commented then that the inventory could be worthless. I did not go on to refer to a cost of destruction which it appears is now inevitable.

[41] However, the inspection in July shows many of the dressers were defective. Eight thousand plus dressers seems like a large number but it must be recalled that Scanwood was to produce more than that every week to comply with its agreements with IKEA. These remaining dressers were being produced in the last few days before Scanwood was placed in receivership.

[42] The quality of the dressers was an issue in June because of the provision in the buy back agreement with respect to quality.

[43] I reluctantly conclude that there are no special circumstances here to convince me I should exercise my discretion to reopen the matter. Even if I did, I

would conclude that the buy back agreement makes the decision about quality of inventory IKEA's decision. Therefore, the appraiser's report suggesting the inventory could be sold is not helpful. It is also not helpful because only one box was opened and, as I have said, because the appraiser did not address the trademark issue satisfactorily.

[44] The authorities cited by RBC, which it says support its argument that equity requires IKEA purchase the inventory, in my view, are not helpful. No one denies that one of the purposes of the *Bankruptcy and Insolvency Act* is to deal equitably with creditors; however, the cases refer to equitably distributing the debtor's assets among its creditors which is not the issue before me.

[45] I therefore conclude, as I have said, reluctantly, that the remaining inventory which IKEA will not purchase must be destroyed. I reiterate the hope I expressed in my June 29 decision that negotiations may result in a different conclusion.

Hood, J.