1994 **S.H. No. 107381**

IN THE SUPREME COURT OF NOVA SCOTIA

BETWEEN:

SUMNER M. FRASER, WILLIAM KITCHEN, WILLIAM MUNDLE and **DR. JAMES COLLINS,** in their personal capacities and as representatives of certain investors in Cavalier Energy Limited (successor to Cavalier Capital Corporation) being all those investors who provided irrevocable unconditional letters of credit or letters of guarantee prior to August 2, 1988 to support a 15 million dollar borrowing by Cavalier Capital Corporation

Plaintiffs

- and -

WESTMINER CANADA LIMITED, WESTMINER HOLDINGS LIMITED, WESTERN MINING CORPORATION HOLDINGS LIMITED, JAMES H. LALOR, PETER MALONEY, WILLIAM B. BRAITHWAITE and **COLIN WISE**

Defendants

DECISION

HEARD: At Halifax, Nova Scotia, before the Honourable Justice D.W. Gruchy on May 31, 1995

DECISION: August 1, 1995

COUNSEL: D.A. Caldwell, Esq., Q.C., Solicitor for the plaintiffs
T.P. Donovan, Esq., Solicitor for the defendants

GRUCHY, J.

This is an application by the defendants to strike that aspect of the plaintiffs' statement of claim taken on behalf of "certain investors in Cavalier Energy Limited (successor to Cavalier Capital Corporation) being all those investors who provided irrevocable unconditional letters of credit or letters of guarantee prior to August 2, 1988, to support a $15 million dollar borrowing by Cavalier Capital Corporation". The defendants claim that this is not an appropriate case for a representative action.

In Nova Scotia representative proceedings must comply with **Civil Procedure Rule** 5.09 which reads:

> 5.09 (1) Where numerous persons have the same interest in a proceeding, not being a proceeding mentioned in rule 5.10, the proceeding may be begun, and, unless the court otherwise orders, continued, but by or against any one or more of them as representing all or as representing all except one or more of them.
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> (2) At any stage of a proceeding under this Rule the court may, on the application of the plaintiff, and on such terms, if any, as it thinks fit, appoint any one or more of the defendants or any other persons to represent all, or all except one or more, of the persons having the same interest in the proceeding, and where, in exercise of the power conferred by this paragraph, the court appoints a person not named as a defendant, it shall make an order under Rule 5.04 adding that person as a defendant.
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> (3) An order given in a proceeding under this Rule is binding on all persons represented in the proceedings as parties, but the court may
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> (a) make it binding on any person not a party to the proceeding;
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> (b) exempt any person represented as a party on the proceeding from any liability under a judgment or order in the proceeding.

To understand the nature of the application it is necessary to examine the statement of claim.

The named plaintiffs are various businessmen. They have brought this action in their personal capacities as investors in Cavalier Energy Limited. They provided irrevocable unconditional letters of credit or letters of guarantee in support of a $15 million dollar borrowing by Cavalier Capital Corporation, the predecessor to Cavalier Energy. They have also brought this action "...as representatives of all other investors in Cavalier Energy who provided irrevocable, unconditional letters of credit prior to August 2, 1988 (hereinafter referred to as the 'letter of credit investors' or 'LC investors'), saving and excepting Terrence D. Coughlan, the Estate of William S. McCartney, Frederick C. Hansen, H. Robert Hemming and Colin J. McDonald (who, together with two others are hereinafter referred to as the 'former Seabright directors')". The excepted individuals were alleged to be substantial shareholders of Cavalier Capital and were also referred to as "Cavalier directors".

The statement of claim identifies and describes each of the defendants and their various relationships relative to the subject matter of this action and in particular their relationship to Seabright Resources Inc. Seabright was in the business of exploring and developing various base metal properties in Canada, primarily in Nova Scotia.

The statement of claim outlines the facts upon which the plaintiffs rely as giving rise to the cause of action. For the purposes of this decision, it is unnecessary to detail the complex factual situation alleged. In essence, the statement of claim sets forth that a company in which the named plaintiffs and others were interested, Cavalier Capital Corporation, borrowed approximately $25 million dollars from the National Bank to acquire the share of Cavalier Energy. Of that borrowing $15 million dollars was guaranteed by irrevocable, unconditional letters of credit from approximately 35 investors, including the named plaintiffs and the group they claim to represent. The $15 million dollars was to be bridge financing and was to be retired or repaid from the proceeds of an intended public offering of investments by Cavalier Capital. That is, each of the plaintiffs was to be released

from the obligation undertaken in the guarantees upon the payment of certain of the funds to be raised by the public offering.

The statement of claim alleges that in the midst of negotiating an underwriting agreement between Cavalier Capital and its proposed underwriter, the defendants Westminer Holdings and Westminer Canada commenced an action in Ontario claiming damages for fraud, deceit, conspiracy and negligent misrepresentation against certain of the Seabright directors and willful misrepresentation as against other former directors of Seabright. The underwriter, in view of that action, inter alia, advised Cavalier Capital to withdraw from the public offering.

As the public offering did not proceed, the bank debt guaranteed by the investors as aforesaid could not be retired as planned. Certain restructuring attempts were made by Cavalier, but they failed and after the amalgamation of Cavalier Energy and Cavalier Capital, the new company eventually went into receivership.

The plaintiffs claim that the Ontario action caused the failure of the initial public offering, a consequence of which was that the plaintiffs were ultimately called upon by their creditor for their shares of the $15 million dollar sum guaranteed. Various actions were commenced in Nova Scotia concerning allegations of conspiracy against the defendants. As a result, this Court, by the decision of Nunn, J. on March 23, 1993, held that the defendants had pursued a course of action or conspiracy with the predominant intention to injure those directors involved in those particular claims. That decision was upheld by the Nova Scotia Supreme Court Appeal Division.

The plaintiffs, in their personal and representative capacities, have claimed damages under various heads against the defendants.

Upon receipt of the statement of claim in this action the defendants demanded and received certain particulars with respect to the identities of the "letters of guarantee"

holders and particulars of the members of the class.

The defendant applied on May 17, 1995, (amended on May 18) "...for an order pursuant to **Civil Procedure Rule** 5.04 that the representative action brought on behalf of the purported class be struck out on the ground that this is not an appropriate case for a representative action and, therefore, the plaintiffs have no status to bring the action on behalf of anyone besides themselves". The notice (amended) also said that in support of the application will be read the affidavit of Myrna L. Gillis, a true copy of which was attached thereto and such other material as counsel may advise.

The plaintiffs have objected to the introduction of affidavit evidence in support of this application. Counsel have agreed that I should dispose of that objection prior to dealing with the application on its merits.

The defendants' interlocutory notice of this application clearly referred to **Civil Procedure Rule 5.04** which reads as follows:

> 5.04 (1) No proceeding shall be defeated by reason of the misjoinder or nonjoinder of any party or person, and the court may determine any question or issue in dispute in a proceeding so far as it affects the rights and interests of any party, saving the rights of any person who is not a party.
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> (2) At any stage of a proceeding the court may, on such terms as it thinks just and either on its own motion or on application,
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> (a) order any party who is not, or has ceased to be, a proper or necessary party, to cease to be a party;
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> (b) order any person, who ought to have been joined as a party or whose participation in the proceeding is necessary to ensure that all matters in the proceeding may be effectually adjudicated upon, be added as a party;
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> But no person shall be added as a plaintiff without his consent signified in writing or in such other manner as the court may order.

The defendants' brief in support of the application says that the application is made under **Civil Procedure Rule** 14.25(a) to strike portions of the plaintiffs' statement of claim. That **Rule** reads:

> 14.25(1) The Court may at any stage of a proceeding order any pleading, affidavit or statement of facts, or anything therein, to be struck out or amended on the ground that,
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> (a) it discloses no reasonable cause of action or defence;
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> (b) it is false, scandalous, frivolous or vexatious;
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> (c) it may prejudice, embarrass or delay the fair trial of the proceeding;
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> (d) it is otherwise an abuse of the process of the court;
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> and may order the proceeding to be stayed or dismissed or judgment to be entered accordingly.
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> (2) Unless the court otherwise orders, no evidence shall be admissible by affidavit or otherwise on an application under paragraph 1(a).

The plaintiffs' brief in connection with this application commenced with the introduction:

> When testing the appropriateness of a class action, especially early in the proceedings, courts have relied almost exclusively on the statement of claim, assuming the allegations of fact to be true unless the applicant demonstrates otherwise. The defendants' application to strike the class action is brought under Rule 14.25(1)(a) which provides, in part, that affidavit evidence is not admissible unless the court otherwise orders.

The plaintiffs continued their pre-application memorandum by references to **Ranjoy Sales and Leasing Ltd. v. Deloitte, Haskins & Sells** (1984), 44 C.P.C. 159; **Korte**

v. Deloitte, Haskins & Sells (1993), 15 C.P.C. (3d) 109; and **Van Audenhove et al v. The Attorney General of Nova Scotia et al** (1993), S.H. No. 102133. Under the authority of **Civil Procedure Rule** 14.25 and the aforesaid cases, the plaintiffs asked that the affidavit and other documents submitted to me with the defendants' application be excluded and the application be considered on the basis of the pleading only.

No defence has yet been filed.

Upon receipt of the plaintiffs' pre-trial memorandum, the defendants further submitted to me by letter of May 24 that I have the requisite discretionary power under both **Rules** 5.09 and 14.25. They say that the materials supplied to me and attached as a bundle of documents to their brief are simply a "reflection of the material disclosed in the previous litigation" and which they believe will be of benefit in establishing the factual context of the application. They concluded their letter of May 24 as follows:

> If the plaintiffs continue to object to the introduction of affidavit evidence following receipt of this letter, we will be prepared to make a preliminary motion for the introduction of affidavit evidence before argument advances in the main matter. In this regard, I ask Mr. Caldwell to provide me with a response to this letter so that we may proceed accordingly.

By letter of May 26, 1995 to Mr. Donovan, Mr. Caldwell indicated that he continued his objection. He quoted particularly Williston and Rolls, **The Law of Civil Procedure** (Butterworths, 1970), Vol. 2 at pp.730-1:

> ...If a motion is brought under the branch of the rule that the pleading discloses no cause of action or answer, only the pleading itself can be looked to and the court has no jurisdiction to consider extrinsic evidence. In determining whether a cause of action or answer is disclosed, the facts alleged in the impugned pleading are assumed to be true, and their improbability is not material. The court should strike out a pleading or dismiss or stay the action only if the facts alleged, which are assumed to be true, disclose no liability or cause of

> action or defence maintainable at law. The power given to the court under Rule 126 (C.P.R. 14.25) and under its inherent jurisdiction to stay a vexatious suit ought to be used sparingly and only in cases which are clear and beyond doubt.

Having cited other authorities, Mr. Caldwell concluded as follows:

> Clearly, the basis for striking out the pleadings will vary depending on which branch of the Rule you choose. Since you gave us notice only of an application under Rule 14.25(1)(a), we have responded to that application. In our view, the materials you have purported to submit in support of the application are clearly "extraneous evidence", and we will object to their introduction on May 31st.

In reply, Mr. Donovan for the defendants has indicated that references to **Rule** 14.25 were merely to provide a mechanism by which the Court could exercise discretion in making an order pursuant to **Rule** 5.09. That is, if I find that this case is not properly a representative action, I should strike the representative portions of this claim pursuant to **Rule** 14.25. Mr. Donovan has submitted that the prohibition of affidavit evidence as contained in **Rule** 14.25(2) relates only to evidence presented to attack the merits of the class action aspects of the statement of claim. He has said that the materials submitted do not go to the merits of the claim advanced in the pleadings but rather provide information as to differences which may exist among the class members and were provided to support the argument that the representative portion of the action should not proceed.

It is my view that the appropriateness of the class is indeed a question which may be addressed before trial. In other jurisdictions courts have frequently addressed this question prior to trial but as many of those jurisdictions do not have the same liberal rules of discovery and take different approaches as to costs, care must be exercised in the application of those cases. Thus, while the consideration of such cases as **Murphy v. Webbwood Mobile Home Estates Limited,** [1978] 19 O.R. (2d) 800 is helpful and instructive, there is not in Nova Scotia the same need as in other provinces to determine the

appropriateness of the class at such an early stage of the proceedings.

The defendant has brought to my attention various Nova Scotia cases in which the representative action aspects of the statements of claim were struck out at a preliminary stage.

In the case, **Inshore Fisherman's Bona Fide Defence Fund Association v. Her Majesty the Queen in Right of Canada** (S.H. No. 93-1803 - February 7, 1994), Justice Nunn of this Court struck the representative action on the basis of affidavit evidence. It is, however, of special importance that such evidence was submitted apparently without objection, and that action involved the question of public interests standing. The affidavit submitted in that case clearly addressed the matter of public interest. Nunn, J. carefully reviewed the facts alleged in the pleadings and affidavits before him in relation to the public interests claimed. He did not address the question whether affidavit evidence should be received and that matter was not apparently raised before him.

In **NsC Corp. and Black v. ABN Amro Bank Canada et al** (1993), 121 N.S.R. (2d) 104, Pugsley, J.A. considered whether a chambers judge should examine affidavits filed in support of a motion to strike pleadings. He referred to the various authorities noted in his decision and concluded, with respect to that aspect of the appeal before him, as follows:

> In the later case of Seacoast Tower Services Ltd. v. MacLean (1986), 75 N.S.R. (2d) 70; 186 A.P.R. 70 (C.A.) Mr. Justice Matthews on behalf of the court, concluded that on an application under rule 14.25(1)(a), the Chambers judge should not consider affidavit evidence.
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> It is important to recognize that the decision of the Chambers judge was based solely on the claims advanced against the two law firms on the pleadings as constituted. The Chambers judge made it clear that he was not making any adjudication of a substantive nature, with respect to the rights of Mr. Black and NsC against the law firms.
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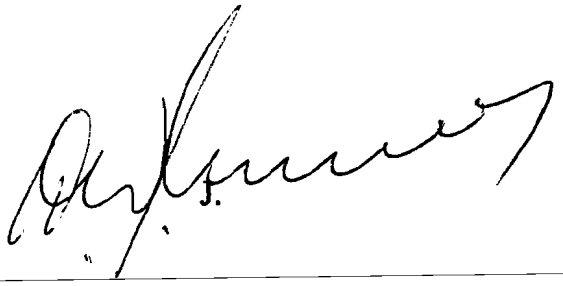
> I conclude on the basis of the foregoing authorities, that the affidavits filed by Mr. Black could not have been considered by the Chambers

> judge on the application under Civil Procedure Rule 15.24 (sic - meaning 14.25), even if they were available in the Chambers file. I find further that no patent injustice follows as a consequence.

The defendants herein filed the affidavit of Myrna L. Gillis without leave of the Court. While Mr. Donovan takes the position that such leave is not mandated by **Civil Procedure Rule** 5.09, the effect of the application however is to strike certain of the pleadings pursuant to **Rule** 14.25(1), for which leave of the Court must be obtained.

While the issues between the parties appear to have been sharpened by virtue of the demands for particulars and their replies, the issues as between the parties are not yet joined by the pleadings; that is, no defence has been filed. In my view, when the issues between the parties have been appropriately joined, or upon the completion of interrogatories and discoveries, by either or both of which processes uncontroverted facts emerge which will support a motion to strike, then affidavit evidence to that effect may be appropriate. At the present time, however, it is my view that the filing of affidavit evidence is premature. At this stage, as well, the filing of an affidavit by one of the parties will undoubtedly lead to the filing of counter-affidavits and cross examination on them. The determination of the issue of the appropriateness of the class would develop into a trial by affidavit - a development which I believe to be undesirable.

I have therefore decided, as I have indicated to counsel, that I will not permit the filing of the affidavits at this juncture. Mr. Donovan, however, is still at liberty to proceed to argue a motion to strike based solely on the pleadings which, at this stage, consist of the statement of claim, the demands for particulars and the replies to those demands.



Halifax, N.S.