Case Name:

Catalyst Fund Limited Partnership II v. IMAX Corp.

RE: Catalyst Fund Limited Partnership II, and IMAX Corporation

[2008] O.J. No. 873

2008 CanLII 8778

Court File No. 07-CL-7163

Ontario Superior Court of Justice
Commercial List

S.E. Pepall J.

March 6, 2008.

(17 paras.)

Civil litigation -- Civil procedure -- Discovery -- Examination for discovery -- Attendance -- Order to attend or re-attend -- In the context of an ongoing oppression action, the application seeking leave to conduct Rule 39.03 examinations after the applicant had already conducted its cross-examinations was dismissed -- Rule 39.02 was there for a reason, importing principles of fairness and economy -- Leave was to be granted sparingly and the moving party had a very high threshold to meet -- A satisfactory explanation for why it did not seek this information prior to the cross-examinations had not been provided -- Ontario Rules of Civil Procedure, Rule 39.02.

Although there were three motions before the court in the context of an ongoing oppression action, in the present endorsement the court disposed only of an application by the applicant Canadian investment fund, which sought leave to conduct Rule 39.03 examinations after it had already conducted its cross-examinations -- There had already been three weeks of cross-examinations of 13 witnesses in five different cities, three states and two countries -- HELD: The applicant was not granted leave -- It was apparent well in advance of the cross-examinations that IMAX had made a misstatement and that Credit Suisse and Bear Stearns might have the relevant information -- Rule 39.02 was there for a reason, importing principles of fairness and economy -- Leave was to be granted sparingly and the moving party had a very high threshold to meet -- A satisfactory

explanation for why it did not seek this information prior to the cross-examinations had not been provided.

Statutes, Regulations and Rules Cited:

Canadian Business Corporations Act, s. 241

Ontario Rules of Civil Procedure, Rule 39.02, Rule 39.03

Counsel:

Robert S. Harrison, C. William Hourigan and Antonio Di Domenico for the Applicant/Moving Party.

R. Paul Steep, Thomas N.T. Sutton and Sarah-Jane Martin for the Respondent.

ENDORSEMENT

1 **S.E. PEPALL J.**:-- There are three motions before me. Two are refusals motions and the other is a request by the applicant for leave to conduct Rule 39.03 examinations after it has already conducted its cross-examinations.

2 The applicant is a Canadian investment fund managed by Catalyst Capital Group Inc. which is not a party. In the offering memorandum, Catalyst Capital Group Inc. describes itself as a private equity investment firm that was founded in 2002 and that "specializes in control and/or influence investments in distressed and undervalued Canadian situations."

3 IMAX is an entertainment technology company incorporated pursuant to the provisions of the CBCA. It is a public company. In August, 2006, IMAX publicly disclosed that it was in the process of responding to an informal inquiry by the SEC regarding its revenue recognition practices.

4 The applicant began to invest in IMAX on October 31, 2006. It holds in excess of $6 million (U.S.) in senior notes issued by IMAX. It became a shareholder in January, 2007.

5 In its amended notice of application, Catalyst requests a section 241 CBCA declaration of oppression (including unfair prejudice and unfair disregard) in that, amongst other things:

1. IMAX put in place a consent solicitation process ("CSP") based on information released by IMAX on the public record that IMAX knew or should have known was false, misleading or incomplete;

2. it prematurely released false or incomplete information to avoid the appearance of being in default;
3. it engaged in a course of conduct designed to suppress or delay information which if provided in a complete and timely manner, would reveal more events of default;
4. it released false or incomplete information knowingly or which it ought to have known;
5. it has announced that none of its previously released financial statements can be relied upon; and
6. it has been unable to put in place sufficient internal financial controls.

6 In the amended notice of application the applicant seeks an order setting aside the consent solicitation, a declaration of default, an order directing an investigation and the appointment of an inspector, and a production order amongst other things.

7 For its part, IMAX maintains that a distinction should be made between the applicant fund which is a limited partnership consisting of sophisticated investors and Catalyst Capital Group Inc., the general manager that is executing an investment strategy. Mr. Steep for IMAX describes Catalyst as a vulture fund that is looking to maximize returns rather than act in the best interests of IMAX, its shareholders or other bond holders. He submits that Catalyst's motions are designed to advance Catalyst's investment strategy and to find a basis to allege default under the trust indenture pursuant to which the notes were issued. Mr. Steep states that the interest payable on the notes is current and the notes trade at par as of the end of January, 2007. He argues that Catalyst is on a fishing expedition designed to trigger a default under the indenture. He urges the Court not to become an unpaid partner in Catalyst's investment strategy.

8 This application engages the oppression remedy. The oppression remedy has a very broad scope and the relief available involves a tremendous amount of discretion. Assuming it qualifies as a complainant, any applicant may be entitled to rely on the provisions of the CBCA and court procedures to pursue its claim. That said, applications can be drafted with a broad brush and our *Rules of Procedure* and the law governing production can easily be manipulated to achieve objectives unrelated to the underlying policy rationale that supports the oppression remedy. Such proceedings can be very expensive, extremely time consuming and distracting, particularly for a company in circumstances of financial distress. The more motions, examinations and time limits, the greater the pressure on the respondent. A judge should not prejudge the merits of an application for oppression. That said, a distinction should be made between that which is truly relevant and that which is speculative - a fishing expedition that is designed to hook the gills and pull at the innards of some respondent with a view to uncovering new grounds of complaint.

9 As mentioned, there are three motions before me. In this endorsement, I am disposing of the leave motion. Endorsements on the other two motions will follow at a later date. The applicant requests letters of request and the issuance of a commission to a New York court reporter to take the

evidence of two New York residents, Mr. R.J. Schwartz, the President and CEO of the brokerage firm, Bear Stearns, and Jared Felt of Credit Suisse First Boston. Bear Stearns is a broker for one of IMAX's noteholders, Plainfield Asset Management, and Credit Suisse was IMAX's solicitation agent for the CSP.

10 In its application, the applicant seeks to set aside the CSP. Under the trust indenture that governs the issuance of the senior notes, IMAX must make timely filings of its financial statements with the OSC and the SEC. If IMAX was late and was served with a notice of default that it was unable to correct within 30 days, it could be faced with an acceleration whereby all $160 million of the senior notes outstanding would have to be paid. IMAX faced delays in filing its financial statements on a timely basis. It accordingly sought the consent of a majority of noteholders to a waiver of its anticipated default. It publicly initiated the CSP on April 3, 2007. Beforehand, it entered an agreement with Plainfield.

11 In that agreement, Plainfield represented that it was in a position to and would vote $53.1 million worth of senior notes in favour of the waiver sought by IMAX. On April 3, 2007, IMAX announced that it had commenced the CSP seeking consents from holders of its senior notes and, based on the Plainfield agreement, stated that two-thirds of the required consents had already been obtained. Although ultimately $53.1 million worth of notes did consent, in fact Plainfield did not control $25.1 million worth of these senior notes.

12 The applicant says, amongst other things, that IMAX's representation was false, oppressive and unfairly prejudicial. The applicant states that the particular factual issues in respect of which the evidence of Messrs. Schwartz and Felt is important are: when did IMAX know that the aforesaid representation was false; did Credit Suisse tell IMAX to recommence the CSP; how did the $25.1 million get voted, and was this as a result of the involvement of Bear Stearns, Credit Suisse or both.

13 At the argument of this motion, both counsel agreed that Rule 39.02 is the applicable Rule. Rule 39.02(1) provides that cross-examinations may take place after a party has served the affidavits on which it intends to rely and after it has completed all examinations under Rule 39.03. Rule 39.02(2) provides that a party who has cross-examined may not conduct an examination under Rule 39.03 without leave or consent. The court shall grant leave where it is satisfied that the party ought to be permitted to respond to any matter raised on the cross-examination with evidence in the form of a transcript of an examination conducted under Rule 39.03.

14 IMAX filed numerous affidavits in response to the notice of application including one from the Managing Director and General Counsel of Plainfield. There have been three weeks of cross-examinations of 13 witnesses in five different cities, three states and two countries. Rule 39.02 is there for a reason. It imports principles of fairness and economy. The examinations that are permissible are explicitly addressed in the Rules. Under Rule 39.2(2), the onus is on the moving party to establish that leave should be granted. In *News Datacom Ltd. v. Love*,[1] the Manitoba Court of Appeal in describing a comparable Rule in its Rules of Procedure, stated that leave should be

granted sparingly and that the moving party has a "very high threshold to meet". I agree.

15 The factors to be considered on a motion for leave pursuant to Rule 39.02(2) are not limited to relevance. They are set forth in *Canadian Royalties Inc. v. Ungava Minerals Corp*.[2] They are: is the evidence relevant; is the evidence responsive to something raised in cross-examination; is there prejudice; and is there a satisfactory explanation for not having included this evidence at the outset.

16 As stated by Stinson J. in *Brock Home Improvement Products Inc. v. Corcoran*,[3]

> Rule 39.02(1) and (2) are an important and integral part of the procedural code governing the conduct of motions and applications. These Rules are designed to place finite limits on the evidentiary element of those proceedings, an element that is all-too frequently time-consuming, expensive and drawn-out. These Rules oblige the parties to consider the issues and to put all relevant evidence forward before embarking upon cross-examination of the opposite party's witnesses. This is the approach mandated by the Rules to achieve the "just, most expeditious and least expensive determination" of motions and applications. Consistent with that approach, it is only in exceptional cases that resort should be had to rule 30.02(2).
>
> I believe that the words "ought to be permitted to respond" found in Rule 39.02(2) impose a burden on a party who seeks leave to show more than an absence of non-compensable prejudice to the opposite party. In my view those words import a requirement for the party who seeks leave under Rule 39.02(2) to provide, by way of evidence on the motion for leave, a satisfactory explanation for its failure to include the proposed additional evidence as part of its pre-cross-examination case. The court should scrutinize carefully the reasons for the omission and the evidence offered in support of that explanation. To approach the issue otherwise undermines the integrity of the evidentiary framework for motions and applications that is mandated by the Rules. Absent some reasonable explanation for the original omission, leave should be refused.

17 Having considered these factors, I have concluded that the applicant should not be granted leave. It was apparent well in advance of the cross-examinations that IMAX had made a misstatement[4] and that Credit Suisse and Bear Stearns might have relevant information. Credit Suisse is identified as the solicitation agent for the CSP in the press release of which the applicant complains and Bear Stearns is identified as Plainfield's broker in the affidavit sworn by Mr. Fritsch of Plainfield and filed by IMAX. The applicant chose to proceed as it did by application and by seeking information relating to Credit Suisse and Bear Stearns through IMAX and Plainfield. This is evident from the notices of examination and amended notices of examination that were served before the cross-examinations. In my view, a satisfactory explanation for why it did not seek this

information prior to the cross-examinations has not been provided. I am not satisfied that the applicant ought to be permitted to respond as it requests and I decline to grant it the order it seeks. Catalyst's motion for leave is dismissed.

S.E. PEPALL J.

1 (2004), 50 C.P.C. (5th) 303.

2 [2003] O.J. No. 4476, 2003 CarwsellOnt 4350 (S.C.).

3 (2002) Carswell Ont. 794.

4 See paras. 2(n) and (p) of the amended notice of application.

---- End of Request ----
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