| *SUMMARY OF CURRENT DOCUMENT* | |
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| **Name of Issuing Party or Person:** | **Mr. Justice Robert M. Hall** |
| **Date of Document:** | **2005 09 02** |
| **Statement of purpose in filing:** | **Reasons for Judgment on Application by PricewaterhouseCoopers Inc. ("PWC") (the "Receiver") for approval of the fees of the Receiver and the Receiver's Counsel.** |
| **Court Sub-File Number:** | **9:12 (Re Sub-File 7:62)** |

**CITATION:** ***In Re Hickman Equipment (1985) Ltd. (In Receivership)*, 2005 NLTD 146**
**DATE: 2005 09 02**
**DOCKET: 2002 01T 0352**

**IN THE SUPREME COURT OF NEWFOUNDLAND AND LABRADOR**
**TRIAL DIVISION**

**IN THE MATTER OF** a Court ordered Receivership of Hickman Equipment (1985) Limited ("Hickman Equipment") pursuant to Rule 25 of the **Rules of the Supreme Court, 1986**, under the **Judicature Act**, RSNL 1990, c. J-4, as amended

**AND IN THE MATTER OF** the **Bankruptcy and Insolvency Act**, c. B-3 of the Revised Statutes of Canada, 1985, as amended (the "BIA")

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**Before: The Honourable Mr. Justice Robert M. Hall**

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**Place of Hearing:** St. John's, Newfoundland and Labrador

**Date of Hearing:** November 29, 2004

**Appearances:** Frederick J. Constantine for the Receiver, PricewaterhouseCoopers Inc.
Thomas R. Kendell, Q.C. for General Motors Acceptance Corporation.
Bruce C. Grant, Q.C. for John Deere Credit Inc.
Geoffrey L. Spencer for Canadian Imperial Bank of Commerce.

**Authorities Cited:**

**Cases Considered:** **Hart Building Supplies Ltd. v. Deloitte & Touche,** [2004] B.C.J. 49 (B.C.S.C. in Chambers**); Montreal Trust Co. v. Churchill Forest Industries (Man.) Ltd.** (1971), 21 D.L.R. (3d) 75 (Man.C.A.); **Hamilton Wentworth Credit Union Ltd. (Liquidator of) v. Courtcliffe Parks Ltd.** (1995), 32 C.B.R. (3d) 303; **Walter E. Heller**, **Canada Ltd. v. Sea Queen of Canada Ltd.** (1974) 19 C.B.R. (N.S.) 252 (Ont. S.C.)

**Statutes Considered:** **Judicature Act**, RSN 1990 c. J-4

**Texts Considered:** *Bennett on Receiverships, (Second Edition)*, Carswell Toronto; I. H. Jacob, *The Inherent Jurisdiction of the Court, Current Legal Problems* 1970

## REASONS FOR JUDGMENT

**Hall, J.**

## Background

[1] This matter arises out of an application by the Receiver for approval of fees and disbursements incurred by it and by its counsel incurred subsequent to April 2003 and not previously approved by this court. The fees of the Receiver (before harmonized sales tax ("HST")) for the period May 1, 2003 to May 31, 2004 total $519,041. The Receiver had also retained the services of two law firms, namely, Merrick Holm and Patterson Palmer, who filed accounts in the amount of $47,558.98 and $136,916.89 respectively.

[2] Subsequent to the filing of the initial affidavits and applications with respect to this matter, both PWC and Patterson Palmer filed supplemental affidavits wherein
they sought approval of their accounts for the period June 1, 2004 to October 31, 2004. The Patterson Palmer accounts totaled $27,010.43. PWC's supplementary affidavits sought approval of further fees and disbursements in the amount of $43,933 (before HST).

[3] On the application for approval of these accounts pursuant to the provisions of the

Receivership Order issued in this matter, counsel on behalf of three secured creditors were heard in opposition to a portion of the accounts related to certain investigations undertaken by the Receiver and research undertaken by the Receiver's counsel relating to potential claims of the Receiver in negligence as against Deloitte & Touche LLP, an international accounting firm, which firm had served as auditors for the bankrupt company Hickman Equipment (1985) Ltd., ("HEL"). I shall refer to this aspect of the receivership as the "Deloitte & Touche matter". Up to the end of May 2004 the Receiver had expended $309,834 in professional fees and disbursements (before HST) related to the Deloitte & Touche matter. Merrick Holm had incurred fees and disbursements in the amount of $9,315.79 in relation to the same matter. Patterson Palmer had not incurred any fees in relation to this matter.

[4] HEL had been incorporated in 1985 and carried on the business of sales, rental and servicing of construction, mining and forestry equipment. It had a series of dealer agreements with a number of heavy equipment suppliers such as John Deere, Ingersoll-Rand, Terex Corporation, Timberjack Corporation, Cedarrapids Inc. and others. From 1985 up to and including 2001, HEL engaged Deloitte & Touche as its sole auditor and financial advisor to provide accounting, auditing, tax and consulting services in respect of its business. In accepting the annual appointment as auditor, Deloitte & Touche apparently undertook to audit HEL's financial statements in accordance with generally accepted accounting standards ("GAAS") and to provide an opinion on whether or not HEL's financial statements presented fairly in all material respects the financial position of HEL as of its year-end of December 31st in each of the years inclusive of 1985 to 2000, and to provide opinions on the results of HEL's operations and its cash lows for each year, all in accordance with Canadian General Accepted Accounting Principles ("GAAP").

[5] In March of 2003 after having conducted a preliminary investigation into the affairs of HEL (at a cost to the receivership of $175,000). PWC came to the conclusion that HEL (and thus PWC as Receiver thereof) may have a cause of action against Deloitte & Touche for professional negligence. In an application heard March 12, 2003, PWC sought the approval of the Court to conduct further investigations into the relationship of Deloitte & Touche with HEL. PWC wished to investigate further the professional services provided to HEL by Deloitte & Touche and any professional negligence arising therefrom which may give rise to a claim by PWC as Receiver of HEL for recovery of the losses which HEL had incurred which losses resulted in its receivership and bankruptcy.

[6] The Receiver's application for Court approval to expend monies of the receivership on a further investigation of the Deloitte & Touche matter was opposed by a number of secured creditors, largely on the premise that the preliminary investigation conducted by PWC at a cost to the receivership of $175,000 had not, in the minds of these secured creditors, produced sufficient results to justify further expenditures being incurred in further investigation. Some of these creditors had, with the knowledge of Deloitte & Touche, advanced

funds to HEL in apparent reliance upon the financial statements prepared by Deloitte & Touche. These creditors therefore considered that there was vested in them in their own right a separate cause of action against Deloitte & Touche and did not wish funds of the receivership (which would come out of the recoveries of the secured creditors) expended on investigations by the Receiver and its counsel which might benefit other creditors or the receivership in general. In the time frame of less than one year during its last year in operation, the actual value of the inventory of HEL (as opposed to its stated value on the books of the company) had shrunk from $90,000,000 to approximately $25,000,000. There were clear appearances of fraud associated with this situation, much of the inventory having been financed several times over without previous security documents having been discharged or those secured creditors being paid. In addition there was evidence of fictitious sales. Against the background of these circumstances I was satisfied that it was in the general interest of the receivership that PWC be authorized to conduct such further investigations and by an Order filed July 28, 2003 it was ordered, *inter alia*, that:

> "4. PWC, in its capacities as Trustee and Receiver of Hickman Equipment, is authorized to take such steps as it may deem necessary or appropriate, including retention of such agents, consultants, advisers, experts, auditors and solicitors to determine whether it had in its capacity as Receiver or Trustee a claim against Deloitte & Touche LLP.
>
> 5. All reasonable costs incurred by PWC for any of the purposes referred to herein, or in exercising the authority provided herein, are proper costs of the Receivership to be allocated and paid in accordance with the provisions of the costs allocation plan unless otherwise ordered by this Court."

[7] Late in 2003, while the investigation authorized by the above-mentioned Order was still continuing, PWC sought leave of the Court to issue a statement of claim against Deloitte & Touche and Deloitte & Touche LLP in order to preserve a limitation period. Such leave was given and a statement of claim was issued, notwithstanding the fact that the investigation was continuing. In the statement of claim PWC alleged that it was apparent from its review that for the financial years 1997 through 2000, inclusive, and perhaps earlier than that, and contrary to the representations of Deloitte & Touche, the audited financial statements of HEL did not fairly represent in all material respects the financial position of HEL for the applicable years in question in accordance with GAAP. Nor were the results of the company's operations and its cash flows for the relevant years in accordance with GAAP in the following regards:

> (a) The value of the inventory was materially overstated for a number of reasons including, but not limited to, accounting practices were not in accordance with GAAP.

(b) There were receivables listed in the books and records of HEL that were fictitious.

(c) HEL, on many units of heavy equipment inventory, had double financed the same item by entering into a series of loan transactions with more than one lender on a single inventory unit for the purpose of granting security to both lenders, purportedly in priority to each other over the unit thereby falsely increasing cash flows.

(d) HEL in some instances had conveyed units of equipment from inventory to buyers while allowing loans that were outstanding on these units to remain unpaid, again falsely increasing cash flows.

(e) HEL purported to enter into a series of transactions with companies that did not exist which resulted in significant losses to HEL as a result of these transactions which were of a nature apparently intended to increase the apparent profitability of the company but which in fact did not increase its profitability but to the contrary concealed operating losses.

(f) HEL had made payments to senior management and directors under a profit based bonus plan arrangement far in excess of the actual amounts that were owed to such individuals given the actual financial status of the company.

[8] The statement of claim went on to allege breaches of contract and professional negligence, the details of which are not necessary to be set out here but included negligent misrepresentation and breach of fiduciary duty.

## **Opposition to Receiver's Accounts**.

[9] The opposition to the passing of the accounts of the Trustee, PWC, and its counsel came from three of the same creditors who had opposed vigorously the further investigation by the Receiver into the Deloitte & Touche matter. Counsel for the Receiver however argues that the Court Order authorizing the investigation was crystal clear. He states that essentially the Court directed PWC to determine whether Deloitte & Touche can be liable to the Receiver and/or HEL. He reminded the Court that there was a huge shortfall in the recoveries when the assets of HEL were realized and that it was necessary in this present application to consider two things:

(1) Had PWC stepped outside of its work mandate in conducting the investigation? and

(2) Was what PWC did necessary and reasonable, particularly with respect to whether or not there were points in time at which PWC should have stepped back from its investigation mandate and asked itself the question whether it should proceed any further with the investigation.

[10] Counsel for PWC asserted that both they and PWC were instruments of the Court. All should be judged by the standard of the Court Order and not by the standards of self-interested

creditors. He pointed out that the potential claims against Deloitte & Touche could extend to as much as $90,000,000. He acknowledged however that it may be a lesser sum but that nonetheless the potential claim was a multimillion dollar one and therefore could be expected, simply on the basis of its large amount, to be seriously contested by Deloitte & Touche and therefore the employment of senior insolvency analysts by PWC in this investigation was justified. He characterizes the arguments of his opponents as being "Monday morning quarter backing".

[11] Counsel for an opposing creditor General Motors Acceptance Corporation objected to the characterization of his client's position as "Monday morning quarter backing". He indicated to the Court that there was nothing appealing to him in having to go through another professional's accounts. However he must do so. He stated that every time he picked up the file he asked himself "How did we get this far apart?" and states that in his view the problem goes right back to when the additional investigation was recommended to the Court. At that stage $175,000 had already been spent and a number of creditors objected to any more being spent. He reminded the Court that he had requested a budget because he feared a blank cheque being given to PWC to conduct the investigation. He pointed out that his objection was not to the various hourly rates of some of the senior level insolvency analysts on the PWC team. His principal point was that the work undertaken was excessive and that his clients had never envisaged the extent of the monies that were ultimately expended. In his view the Receiver should have come back to the Court with a request for further directions at the time when it sought leave to issue the statement of claim as against Deloitte & Touche in December. He pointed out that at that time the Receiver had expended $100,000 and that this was an appropriate time to review the important features of the claim as were fleshed out in the statement of claim. He contended that at this point the Receiver's investigation was essentially completed. He questioned why the Receiver did not come back to Court demonstrating to the Court the progress which it had made, what it envisaged it had to do further with respect to the matter and what professionals it envisaged would need to be retained or assigned to the file. He states that as a result of doing that the Court could then ask the question "Are we all on the same page?". In his view the Receiver's fees in this regard (and those of its counsel related to this aspect of the file) ought to be approved only for those incurred up to December 31, 2003, or at the very latest by the end of February 2004 when the decision of the British Columbia Supreme Court in **Hart Building Supplies Ltd. v. Deloitte & Touche,** [2004] B.C.J. 49 (B.C.S.C. in Chambers**)** was issued. The decision in **Hart** was in an application by Deloitte & Touche to dismiss a claim against it for failing to discover and report to Hart a serious overstatement of its inventory value. A director who held 15% of the shares of Hart was aware of the overstatement and allowed it to continue. The Court ruled in favour of Deloitte & Touche on the basis that the director was a directing mind of Hart and his misrepresentations had allowed it to stay in operation.

[12] General Motors Acceptance Corporation is supported by counsel for John Deere Credit Inc. and Canadian Imperial Bank of Commerce. Counsel for John Deere pointed out the wording of the Order which referenced the Receiver's fees and disbursements as being required to be "reasonable". Implicit in this word, he argues, is the concept of "cost containment". In his view the intent of the Order was for the Receiver to focus on what was to be the benefit to the receivership in proceeding any further. He argues that of December 31st that picture was reasonably clear, both from a legal and an investigatory point of view and the Receiver ought to have come back to the Court for further

instructions.

## Decision.

[13] In Court appointed receiverships, the Court, in appointing a receiver has an inherent jurisdiction as well as ancillary powers necessary to make that jurisdiction effective. (See **Montreal Trust Co. v. Churchill Forest Industries (Man.) Ltd.** (1971), 21 DLR (3d) 75 (Man.C.A.), at para. 19 where the Court cited with approval I. H. Jacob, *The Inherent Jurisdiction of the Court, Current Legal Problems* 1970, pp. 23 - 52 who at p. 51 stated:

> "In this light, the inherent jurisdiction of the court may be defined as being the reserve or fund of powers, a residual source of powers, which the court may draw upon as necessary whenever it is just or equitable to do so, and in particular to ensure the observance of the due process of law, to prevent improper vexation or oppression, to do justice between the parties and to secure a fair trial between them.")

[14] Section 105(1) of the **Judicature Act**, RSN 1990 c. J-4 states:

> "A mandamus or an injunction may be granted, or a receiver appointed, by an order of the court, in all cases in which it appears to the court to be just or convenient that the order should be made."

In **Hamilton Wentworth Credit Union Ltd. (Liquidator of) v. Courtcliffe Parks Ltd.** (1995), 32 C.B.R. (3d) 303, the Court observed:

> "The purpose of a general receivership is to enhance and facilitate the preservation and realization of the assets for the benefit of all of the creditors, including secured creditors ... The debtor's property comes under the administration and supervision of the court, through the receiver and manager, which is the agent of the court and not of the creditors at whose instance it is appointed. This being the case, the integrity of the receivership process requires that the court perform its role as supervisor in connection with what happens to the property that comes under its administration."

[15] In *Bennett on Receiverships, (Second Edition)*, Carswell Toronto, at p. 474, the author concludes that Courts review the following criteria in setting a fee for the receivership:

(1) the nature, extent and value of the assets;

(2) the complications and difficulties encountered by the receiver;

(3) the degree of assistance provided by the debtor;

(4) the time spent by the receiver;

(5) the receiver's knowledge, experience and skills;

(6) the diligence and thoroughness displayed by the receiver;

(7) the responsibilities assumed;

(8) the results of the receiver's efforts; and

(9) the cost of comparable services.

[16] The author at p. 475 acknowledged that the receiver's efforts in maximizing the realization may not be successful and the receiver may not produce the highest dollar but that the receiver should nevertheless not necessarily be punished where, with the benefit of hindsight, the actions did not yield the greatest realization. Nor should the Court penalize the receiver for taking steps to preserve the property for sale, if the sale price turns out to be unproductive. In quoting from **Walter E. Heller**, **Canada Ltd. v. Sea Queen of Canada Ltd.** (1974) 19 C.B.R. (N.S.) 252 (Ont.S.C.):

> "The Court must look 'at the number of hours in relation to what was done and the length of time involved'. There should be some correlation of the cost to the benefits derived from the receivership although that may not be possible if the receiver is required to spend considerable time in administering the estate. On a *quantum meruit* approach, the Court does not penalize the receiver in taking steps that are unproductive, but are necessary for the preservation and sale of the assets, as compared to the cost/benefit approach."

[17] I have been involved in hearings with respect to this bankruptcy and receivership for over three and a half years. I am satisfied based upon that experience alone that the reasons for this bankruptcy and receivership are both complex and difficult. The investigation thereof has required a great degree of professional knowledge, experience and skill on the part of the Receiver. In this regard I am satisfied that the Receiver has exercised all due diligence and acted totally in accordance with the Court's authorization to investigate the Deloitte & Touche matter. Its recommendations have been received by the Court as have the recommendations of its counsel. I am satisfied that the recommendations are both thorough and reasonable. The costs incurred stem entirely from the fact that the receivership is a large one and has resulted from a great number of complex transactions skillfully entered into by the perpetrators thereof with a view to misstating the financial position of the company. I am further satisfied that the Receiver's investigations of the responsibility of

Deloitte & Touche (if any) in not detecting these schemes has been competent and thorough. Naturally all of the creditors would prefer that the large costs of these investigations and opinions not have arisen. That however does not render the investigations and opinions unreasonable or contrary to the mandate granted by the Court Order. Considerable recovery possibilities potentially exist in the action against Deloitte & Touche and in this regard I am satisfied that the expenditures with respect to the investigation and the opinions of legal counsel are in compliance with the Court Order and the fees and disbursements of the Receiver and the Receiver's counsel in relation thereto therefore ought to be approved. I am not satisfied that the B.C. Supreme Court decision in the **Hart** matter in January 2004 should have caused the Receiver and its counsel to cease their work. **Hart** turned upon a specific finding that a director was a "directing mind" of Hart and had participated in the misrepresentation. I am satisfied that there is a real issue to be tried in this matter as to who were the directing minds of HEL and did those directing minds participate in the misfeasance. The views of the opposing creditors on this issue are not developed before this Court. They appear to have jumped at the **Hart** decision as a vindication of their initial views. I am not satisfied that the factual or legal state of affairs in the HEL matter is nearly as clear cut or simplistic as suggested by the creditors relying on **Hart**.

[18] I therefore order that the accounts of the Receiver, PricewaterhouseCoopers Inc., and their counsel, Merrick Holm and Patterson Palmer, to October 31, 2004 be approved as filed with the Court.

Justice