WARREN INDUSTRIAL FELDSPAR CO. LTD V. UNION CARBIDE CANADA LTD. (MOTION FOR SECURITY FOR COSTS)

Warren Industrial Feldspar Co. Ltd. v. Union Carbide Canada Ltd. et al.

54 O.R. (2d) 213

[1986] O.J. No. 2364

Ontario

High Court of Justice

Trainor J.

March 26, 1986.

Civil procedure — Costs — Security — Corporation — Impecuniosity — No onus on defendant to prove impecuniosity — Plaintiff not entitled to relief on basis of impecuniosity where plaintiff alleges it has sufficient assets — Rule 56.01(d).

The defendants moved pursuant to rule 56.01(d) for an order for security for costs against the plaintiff corporation, alleging that there was good reason to believe that the plaintiff had insufficient assets to answer for costs if ordered to do so. The motions court judge dismissed the

application, holding that there was an onus on the defendants to prove the plaintiff ‘s want of assets, and that because the plaintiff appeared to have a strong case it would be unjust to make an order which might thereby deprive it of its right to proceed. The defendants appealed. **Held,** the appeal should be allowed and an order for security for costs granted. There is no onus on the defendants to prove that the plaintiff has insufficient assets. The defendant must merely show good reason to believe that the plaintiff has insufficient assets. The motions court judge also erred in refusing to order security because the order would deprive the plaintiff of the right to proceed. The plaintiff had stated that it had sufficient assets, led no evidence to prove its impecuniosity, and did not itself seek equitable relief from posting security for costs. The merits of the plaintiff ‘s case should not have been considered as the plaintiff did not take the position that it was impecunious and that an order for security would be therefore unjust.

Smallwood v. Sparling et al. (1983), 40 O.R. (2d) 796; affd 42 O.R. (2d) 53, 34 C.P.C. 24, *folld*

Other cases referred to

RCVM Enterprises Ltd. v. Int’l Harvester Canada Ltd. et al. (1985), 50 O.R. (2d) 508, 50 C.P.C. 278; Brunswick Printing Ltd. et al. v. Centennial Office Equipment; Ken Sears Ins. Ltd.

et al. (third parties) (1984), 59 N.B.R. (2d) 243,

1 C.P.C.

(2d) 66; Willowtree Investments Inc. et al. v. Brown (1985),

48 C.P.C. 150; McCormack v. Newman et al. (1983),

35 C.P.C.

298; City Paving Co. Ltd. v. City of Port Colborne et al.

(1985), 3 C.P.C. (2d) 316; Hawaiian Airlines, Inc. v.

Chartermasters, Inc. et al. (1985), 50 O.R. (2d) 575,

50 C.P.C.

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Rules and regulations referred to

Rules of Civil Procedure, rules 37.06(c), 37.10(3), (4),

39.01(1), 39.03, 56.01(d)

Rules of Practice, Rule 373

APPEAL from an order of the motions court judge dismissing an application by the defendants for an order for security for costs.

D. Peter Best, for appellants.

Hugh A. Doig, Q.C., for respondent.

TRAINOR J.:— This is an appeal from an order dismissing the motions of the defendants for security for costs under rule 56.01(d) of the Rules of Civil Procedure.

56.01 In an action where it appears that,

. . . . .

(d) the plaintiff is a corporation or a nominal plaintiff, and there is good reason to believe that the plaintiff has insufficient assets in Ontario to pay the costs of the defendant if ordered to do so;

. . . . .

the court on motion by the defendant may make such order for security for costs as is just.

The respondent (the plaintiff), Warren Industrial Feldspar Company Ltd. ("Warren"), is in the business of exploring, developing and marketing industrial minerals, which it extracts from quarries under licence agreements.

The appellant (the defendant), Union Carbide Canada Limited ("Union Carbide"), agreed, by two purchase orders, to purchase a total of 22,000 metric tons of high-purity quartz from Warren. Warren contracted with the defendant, Alexander Centre Industries Limited ("Alexander Centre"), to have it

wash, screen and crush the quartz to be supplied to Union Carbide.

The defendant, Elkem Metal Canada Inc. (“Elkem”), subsequently purchased a portion of Union Carbide’s business assets, and the second purchase order referred to above was assigned to Elkem. After disputes between Union Carbide and Warren regarding the quality and quantity of the quartz supplied Elkem purported to cancel the second purchase order. There is a dispute as to whether Elkem was entitled to do so.

With respect to the quartz supplied under the first purchase order, Union Carbide alleges that an insufficient amount of quartz was delivered and that portions of the quartz were improperly washed or sized. Union Carbide refused to pay the full contract price and deducted various charges from the amount owing to the plaintiff. Warren is suing Union Carbide for breach of contract, and is claiming against both Union Carbide and Elkem for wrongful rescission of the second purchase order.

The plaintiff is also suing Alexander Centre, claiming that any deficiencies in the quartz were due to its breach of, or negligence in performing, its contract with Warren. Alexander Centre is counterclaiming for various costs incurred in the crushing, screening and washing of the quartz. The plaintiff has not filed a defence to this counterclaim.

Finally, it should be mentioned that $60,000 owed by Union Carbide to the plaintiff in connection with the quartz supplied was paid to Warren and Alexander Centre jointly, by agreement, and is being held in trust by counsel for both parties. The fund (which now totals approximately $65,000, including interest) is to be disposed of in accordance with any settlement reached by the parties, or the judgment of the court.

On their motions for security for costs under rule 56.01(d) (which were heard together) the defendants took the position that the plaintiff was a corporation with insufficient assets in Ontario to pay the costs of the defendants, if ordered to do so. They adduced evidence of various debts and unsatisfied judgments outstanding against the plaintiff as well as a transcript of the plaintiff ‘s judgment debtor examination. That transcript contains statements by the plaintiff ‘s representative, Mr. Eglon Rose, indicating that Warren’s only assets are a 1976 Honda Civic and various office supplies.

The plaintiff on the motion for security took the position that it was not impecunious, but had assets with a potential worth of approximately $7,000,000 in the form of contracts for the extraction of industrial minerals which were still being negotiated. The plaintiff refused to disclose particulars regarding these negotiations on the ground that disclosure of

such confidential information would damage its position vis-a-vis its competitors.

In dismissing the defendants' motions for security for costs, the motions court judge held that the plaintiff probably had a good cause of action against at least one of the defendants, and would probably recover more than enough at trial to pay costs, if ordered to do so. The judge also found that large sums of money had been withheld from the plaintiff by the defendants and that, under such circumstances, it would be unfair to require the plaintiff to post security for costs. He also said that the defendants had failed to prove that the plaintiff had insufficient assets in Ontario to answer for costs. The judge below concluded that security for costs should not be ordered where it would deprive the plaintiff of what was probably a valid cause of action.

The defendants now advance four main grounds of appeal. Firstly, they argue that the motions court judge erred in requiring the defendants to prove that the plaintiff has insufficient assets to answer for costs, rather than requiring them to show reasonable grounds for believing that to be the case.

Secondly, they state that the judge improperly based his decision regarding security for costs entirely on his assessment of the merits of the plaintiff 's case.

Thirdly, the defendants argue that the learned judge was incorrect in finding that an order requiring the plaintiff to post security for costs would deprive it of a valid cause of action. They contend that this holding is inconsistent with his earlier finding regarding the plaintiff ‘s assets, and with the plaintiff ‘s own assertion that it is not impecunious. They also argue that the effect of the order is to grant the plaintiff relief on the basis of its impecuniosity and the equities in its favour, although no equitable relief was requested by the plaintiff and no evidence was led by the plaintiff to support the granting of such relief.

Finally, the defendants state that the judge based his decision on certain documents which were not properly before him because they were filed by the plaintiff without being included in an affidavit, as required by rule 39.01(1).

The plaintiff takes the position that the wording of rule 56.01(d), which allows security for costs to be ordered “as is just”, confers discretion to consider the merits of a case on a motion for security for costs. An appellate court should not interfere with a judge’s exercise of discretion on a motion for security for costs (including his discretion to consider the merits of the case), unless it is clearly shown that it was exercised on wrong principles.

The plaintiff also argues that the opening words of cl. (d) of rule 56.01 (which require the plaintiff to be “a corporation

or a nominal plaintiff “) should be read conjunctively, so as to prevent the defendants from omitting the words “or a nominal plaintiff ” and merely seek security for costs from the plaintiff as a “corporation”.

Finally, it takes the position that the documents objected to by the defendants were properly before the court, although not contained in an affidavit, because they were referred to in the defendants’ notice of motion and motion records and were included in the plaintiff ‘s motion record.

The main issues in this appeal regarding the interpretation of rule 56.01(d) are as follows:

1. What onus must the defendants satisfy to be entitled to anorder for security for costs?
2. Under what circumstances, if any, can a plaintiff berelieved of the obligation to post security for costs once the defendant has established an entitlement to security, and what evidence is required to obtain such relief?
3. To what extent can the merits of a case be considered on amotion for security for costs?

With respect to the first issue, regarding the defendants’ onus of proof under rule 56.01(d), the wording of the rule requires that the defendant show “good reason to believe that the plaintiff has insufficient assets in Ontario to pay the costs of the defendant, if ordered to do so” (emphasis added). The defendants argue (based on the motions court judge’s statement that “I am not satisfied that the defendants have

proved that the plaintiff has insufficient assets") that the learned judge incorrectly placed a heavier onus on the defendants, to prove the plaintiff 's impecuniosity, than the rule requires.

The defendants rely on the case of RCVM Enterprises Ltd. v. Int'l Harvester Canada Ltd. et al. (1985), 50 O.R. (2d) 508, 50 C.P.C. 278, which involved a motion for security for costs under rule 56.01(d), in support of which the defendants led evidence of writs of execution outstanding against the plaintiff and of the plaintiff 's failure to file corporate returns in Ontario. Master Clark held that such evidence established good reason to believe that the plaintiff had insufficient assets in Ontario and prima facie entitled the defendants to an order for security for costs unless good reason to the contrary was shown. A similar conclusion was reached by the New Brunswick Court of Queen's Bench in the case of Brunswick Printing Ltd. et al. v. Centennial Office Equipment; Ken Sears Ins. Ltd. et al. (third parties) (1984), 59 N.B.R. (2d) 243, 1 C.P.C. (2d) 66, involving a motion under rule 58.01(d) of the New Brunswick Rules of Court (which is nearly identical to Ontario rule 56.01(d)). There, evidence of a sheriff 's certificate and unsatisfied judgments outstanding against the defendant was considered prima facie proof that the

defendant had insufficient assets to pay the costs of the third parties, if ordered to do so.

Finally, the defendants rely on the case of Smallwood v. Sparling et al. (1983), 40 O.R. (2d) 796, affirmed 42 O.R. (2d) 53, 34 C.P.C. 24, which involved an application under old Rule 378 for increased security for costs from a plaintiff living in a reciprocating jurisdiction. On appeal from the order of Master Peppiatt, Galligan J. held that the defendant was prima facie entitled to an order for security for costs upon proof that the plaintiff resided out of the jurisdiction. Galligan J. further held that the onus then shifted to the plaintiff to prove that he had sufficient assets to make such an order unnecessary, stating (at p. 57) that:

> In most cases the facts which would cause a discretion to be exercised in the plaintiff ‘s favour are likely to be uniquely within the plaintiff ‘s own knowledge. … It does not strike me as reasonable to cast a burden upon a defendant who has a prima facie right to security to elicit evidence that the plaintiff does not have sufficient assets within the plaintiff ‘s jurisdiction of residence.

Although rule 56.01(d) clearly requires the defendants to establish that there is good reason to believe that the plaintiff has insufficient assets, Galligan J.’s observations

regarding the difficulties which a defendant faces in attempting to prove the state of the plaintiff ‘s assets are nevertheless relevant.

The plaintiff is correct in asserting that a judge’s exercise of discretion should not be interfered with on appeal unless it is clearly shown to have been exercised on wrong principles or a misapprehension of the facts. However, based on the wording of rule 56.01(d) and on the case-law canvassed above, such an error in principle was made in the present case, in requiring the defendants to prove, rather than merely establish good reason to believe, that the plaintiff had insufficient assets to answer for costs. Imposing such a heavy onus on the defendant is inconsistent with the plain wording of rule 56.01(d) and, as was stated by Galligan J. in Smallwood v. Sparling, supra, unfairly requires the defendant to prove something which is uniquely within the knowledge of the plaintiff.

The defendants have satisfied the onus of showing good reason to believe that the plaintiff has insufficient assets to answer for costs. They have adduced evidence of over $100,000 worth of debts and unsatisfied judgments outstanding against the respondent, most of which are admitted by the plaintiff in its factum for this appeal. The defendants also rely on statements by Eglon Rose, made as the plaintiff ‘s representative during a judgment debtor examination on February 16, 1984, to the effect

that the plaintiff ‘s only assets are a 1976 Honda Civic and various office supplies. Although the respondent asserts that it has assets with a potential worth of $7,000,000 in the form of contracts which are currently being negotiated, the plaintiff has adduced no evidence in support of this claim and has not attempted to explain the statements of Eglon Rose, referred to above. Having established that the plaintiff is a corporation and that there is good reason to believe that it has insufficient assets to answer for costs, the defendants are prima facie entitled to an order for security for costs. This approach is consistent with the wording of rule 56.01(d), and with the decision of Master Clark in RCVM Enterprises Ltd. v. Int’l Harvester, supra (with whom I agree in this regard).

Once the defendants are found to be entitled to security for costs, an issue arises as to whether the plaintiff can avoid the obligation to post security. This issue was addressed by Master Clark in the RCVM Enterprises case, where it was held that the plaintiff has two options. It may lead evidence to show that it has sufficient assets in Ontario to make an order for security for costs unnecessary. Alternatively, it may rely on its own impecuniosity, lead evidence to substantiate it, and show why justice demands that it be allowed to proceed without posting security, notwithstanding its impecuniosity. This approach is similar to that taken in Smallwood v. Sparling, supra; Willowtree Investments Inc. et al. v. Brown (1985), 48

C.P.C. 150 at p. 155, and McCormack v. Newman et al. (1983), 35 C.P.C. 298 at p. 301.

In both the RCVM Enterprises case, and the later case of City Paving Co. Ltd. v. City of Port Colborne et al. (1985), 3 C.P.C. (2d) 316, which also involved a motion under rule 56.01(d), some doubt was expressed as to whether a plaintiff could avoid posting security for costs on the ground of its own impecuniosity, since it is that very impecuniosity which is the basis for ordering security for costs under rule 56.01(d). In earlier case-law where security for costs was ordered on a different basis it was well-settled that the plaintiff could rely on his own impecuniosity to avoid posting security. In Smallwood v. Sparling, Galligan J. states (at p. 56) that:

It has been recognized in Ontario that it lies within the proper exercise of judicial discretion to decline to order a non-resident to post increased security, or to order nominal security if, because of impecuniosity, the requirement of security for costs might work an injustice by wrongfully denying a worthy plaintiff the opportunity of having his or her cause adjudicated upon.

. . . . .

While the discretion to decline to order security for costs … because of the impecuniosity … is one which must be

exercised with caution and on material that shows special circumstances, it is a very important discretion …

Rule 56.01(d) differs from its predecessor, Rule 373, in that (among other things) it provides for the posting of security for costs by a corporation shown to have insufficient assets in Ontario, and allows the court to make such order for security for costs "as is just". I am of the view that these changes do not remove the court's discretion to relieve an impecunious plaintiff from posting security for costs where it would deprive the plaintiff of a valid cause of action. The inclusion of the words "as is just" preserve the court's discretion to grant such equitable relief, upon proof of special circumstances which would make an order for security for costs unjust.

In the present case, it appears that the motions court judge relieved the plaintiff of its obligation to post security on the basis of its impecuniosity, stating that, "I do not think that this rule (56.01(d)) should be used to deprive a plaintiff of what is probably a valid cause of action". This is inconsistent with his earlier holding that the defendants had failed to prove that the plaintiff had insufficient assets in Ontario. If the plaintiff did have sufficient assets, posting security would not deprive it of its cause of action, and any financial difficulties caused by the order could be alleviated

by allowing security to be posted in the form of a bond or letter of credit.

A further difficulty with the decision in the present case is that it has the effect of granting the plaintiff equitable relief on the basis of its impecuniosity, notwithstanding the fact that the plaintiff stated it had sufficient assets and did not request or lead evidence to support such equitable relief. The case-law is unanimous in holding that in order to obtain relief on the basis of impecuniosity, a plaintiff must lead evidence to demonstrate its impecuniosity and to show why justice demands that it be allowed to proceed without posting security for costs, notwithstanding that impecuniosity. It was therefore an error in principle in the present case to grant the plaintiff relief from posting security for costs on the ground that it would deprive the plaintiff of a valid cause of action in the absence of evidence of both impecuniosity and the special circumstances which would make such an order inequitable.

The final issue which arises with respect to the interpretation of rule 56.01(d) is the extent to which the merits of a case may be considered on a motion for security for costs. Under old Rule 373, no such consideration of the merits was permitted unless specifically provided for in a rule or statute: Re Agar, [1957] O.W.N. 208. As noted earlier, rule 56.01(d) differs from its predecessor in that it provides for

security for costs to be ordered, “as is just”. This has been recently interpreted in Hawaiian Airlines, Inc. v. Chartermasters, Inc. et al. (1985), 50 O.R. (2d) 575, 50 C.P.C. 224, to permit the court to consider the merits of a case on a motion under rule 56.01(d). In that case, Master Sandler stated (at p. 577 O.R., p. 227 C.P.C.) that:

> I am unable to reasonably conclude at this stage, that the merits of this action point strongly in one direction or the other, and thus, in this particular case, I have not made a finding on the merits in exercising my discretion. In most cases, it will be impossible to reasonably come to any conclusion on where the merits of a case lie and the “merits” will be a neutral factor. But I do hold that under the new rules, this can be an appropriate consideration.

I am in agreement with Master Sandler that the inclusion of the words “as is just” in rule 56.01(d) permits the court to consider the merits of a case in determining whether to order security for costs. It appears to me that it would only be appropriate or necessary to consider the merits of a case where the defendant has established a prima facie case of entitlement to security for costs, and the plaintiff seeks to avoid posting security on the basis of its own impecuniosity. In such a case, the court may consider the merits of the plaintiff ‘s case to determine whether it has a valid cause of action which it

should be permitted to litigate without posting security and to assess its prospects for success at trial.

It is this consideration of the merits for the purpose of assessing the parties' prospects for success at trial which is problematic. As was noted by Master Sandler in Hawaiian Airlines, a case will seldom be sufficiently clear-cut to come to a conclusion on the merits upon an interlocutory motion. Furthermore, it is not desirable for the merits of a case to be tried on a motion for security for costs, particularly where the action is complex.

The motions court judge's refusal to order security for costs in the present case was partly based on his assessment of the merits of the plaintiff 's case, and on his conclusion that the plaintiff would probably recover enough at trial to answer for costs. It would appear that such a consideration of the merits was not appropriate in that the plaintiff did not argue that it was impecunious and did not lead evidence to show that an order for security for costs would be unjust. It was therefore premature to consider whether the plaintiff was likely to succeed at trial. I am also of the view that the present case is too complex to reach any conclusion on the merits on a motion for security for costs.

I wish to deal briefly with the respondent's argument that the words "corporation or nominal plaintiff " in rule 56.01(d) should be read conjunctively, so as to require a defendant to

seek security for costs from the plaintiff as both a "corporation or nominal plaintiff ". This interpretation is contrary to the plain wording of rule 56.01(d) which permits a defendant to seek security for costs from a plaintiff corporation which has insufficient assets in Ontario to answer for costs. The defendant need not, in addition, prove that the corporation is also a nominal plaintiff.

Lastly, it has been argued by the defendants that certain documents filed by the respondent were not properly before the court because they were not included in an affidavit, as required by rule 39.01(1), which provides as follows:

> 39.01(1) Evidence on a motion or application may be given by affidavit unless a statute or these rules provide otherwise.

The plaintiff takes the position that rules 37.06(c), 37.10(3) and 37.10(4) provide for the admissibility of documentary evidence, on a motion, otherwise than by affidavit. The plaintiff argues that documentary evidence not included in an affidavit will be admissible on a motion if it is included in the plaintiff 's motion record. I cannot accept this argument. The proper practice, in adducing documentary evidence on a motion, is to exhibit the documents to an affidavit or to introduce the document into evidence upon the examination or cross-examination of a witness pursuant to rule 39.03. Although there are various statutory provisions allowing certain

documents to be proved by the use of a certified copy, absent such a provision, documents should be proved by affidavit or oral evidence and cannot be simply filed with the court for use on a motion.

In conclusion, I find that the motions court judge erred in:

1. Imposing an onus upon the defendants to prove, rather than show good reason to believe, that the plaintiff had insufficient assets to answer for costs, if ordered to do so;

2. refusing to order security for costs on the basis of the plaintiff ‘s impecuniosity, notwithstanding that the plaintiff stated that it had sufficient assets, led no evidence to prove its impecuniosity and did not seek equitable relief from posting security for costs, and

3. considering the merits of the plaintiff ‘s case where the plaintiff did not take the position that it was impecunious and that an order for security for costs would be unjust.

The defendants’ estimated costs are as follows:

1. Alexander Industries –$ 32,575.65
2. Union Carbide –40,706.75
3. Elkem –30,157.00 $103,439.40

The estimated trial time and the amount of the estimated costs were unchallenged in the material and argument. However,

I would not order posting of security in the full amounts estimated for several reasons.

Firstly, the trust fund of $65,000 is at this moment a joint asset. The plaintiff ‘s claim against Alexander, even in the absence of a defence to counterclaim, places Alexander’s entitlement to the fund directly in issue. However, the plaintiff and Alexander agreed that the trust would be used to respond to the judgment and I infer not the costs. As a consequence only the sum of $10,000, being the excess of the trust fund over and above the counterclaim, can be considered as security for costs.

Secondly, the substantial issues raised involve the plaintiff, and the defendants Alexander and Union Carbide. Elken’s right to cancel the purchase order appears to me to depend on the resolution of issues in the action against Union. The cross-claim made by Union against Elkem has been discontinued. Counsel for Union and Elkem should give serious consideration to one counsel acting for both defendants in order to avoid unnecessary duplication of effort.

The estimated costs total $104,439.40. In this case it is appropriate to reduce that total by one-half and to deduct from that sum, the amount of $10,000 already held in trust.

The appeal is allowed. The plaintiff is to post security for costs in the total amount of $42,219.70 in cash, by bond or by

other instrument satisfactory to the parties or approved by a judge of the District Court. If the defendants are awarded costs, such costs shall be paid out of the security and the $10,000 fund on a pro rata basis after taxation.

Costs of this appeal to the defendants in the cause.

Appeal allowed; order accordingly.