

**SUPERIOR COURT OF JUSTICE**

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Date: June 30, 2011

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**RE: ONEX CORPORATION ET AL. v. AMERICAN HOME  
ASSURANCE COMPANY ET AL.  
DOCKET: CV-08-00365387**

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Please contact Gladys Gabbidon at (416) 327-5052 if you do not receive all pages. Thank you.

CITATION: Onex v. American Home, 2011 ONSC 1142

DATE: 20110630

DOCKET: CV-08-00365387

ONTARIO

SUPERIOR COURT OF JUSTICE

BETWEEN:

ONEX CORPORATION, GERALD W. SCHWARTZ, CHRISTOPHER A. GOVAN, MARK HILSON AND NIGEL WRIGHT

Plaintiffs

- and -

AMERICAN HOME ASSURANCE COMPANY, BRIT SYNDICATES LTD. (LLOYD'S SYNDICATE 2987) AND HERITAGE MANAGING AGENCY LIMITED (LLOYD'S SYNDICATE 3245), XL INSURANCE COMPANY LIMITED, LIBERTY MUTUAL INSURANCE COMPANY, LLOYD'S UNDERWRITERS SYNDICATES NO. 2623, 0623, 0033 AND AIG EUROPE (UK) LIMITED, HOUSTON CASUALTY COMPANY

Defendants

*Geoffrey D.E. Adair, Q.C. and Alexa Sulzenko* for the Plaintiffs

*Marcus B. Snowden and Fabia Wong* for the Defendant American Home Assurance Company

*Allan L.W. D'Silva, Ellen M. Snow and Paloma Ellard* for the Defendants Brit Syndicates Ltd. (Lloyd's Syndicate 2987) and Heritage Managing Agency Limited (Lloyd's Syndicate 3245), XL Insurance Company Limited, Liberty Mutual Insurance Company and Houston Casualty Company

HEARD: February 14, 15, 16, 17 and 18, 2011

L. A. PATTILLO J.

Introduction

[1] On May 10, 2005, Richard M. Kipperman, in his capacity as Trustee for the Magnatrx Litigation Trust, commenced an action in the United States District Court for the Northern District of Georgia (the "Kipperman Action") against, amongst others, the Plaintiffs in this action, Onex Corporation ("Onex"), Gerald W. Schwartz ("Schwartz"), Christopher A. Govan ("Govan"), Mark Hilson ("Hilson") and Nigel Wright ("Wright") claiming damages in excess of \$600,000,000. The Complaint related to the operations of Magnatrx Corporation ("Magnatrx"), a former subsidiary of Onex, and alleged that the conduct of the defendants resulted in Magnatrx and its subsidiaries becoming "hopelessly insolvent, inadequately capitalized and not able to pay their debts."

[2] To date, Onex has expended approximately \$35 million USD in the joint defence of the Kipperman Action with Schwartz, Govan, Hilson and Wright.

[3] The Plaintiffs commenced this action by statement of claim dated October 10, 2008 claiming reimbursement for their defence costs in the Kipperman Action pursuant to certain directors' and officers' ("D&O") liability insurance policies issued by the defendant American Home Assurance Company ("American Home") and excess D&O insurance policies issued by the remaining Defendants to Onex (the "Action").

[4] The Plaintiffs move for summary judgment in the Action requiring American Home to pay defence costs they have incurred defending the Kipperman Action pursuant to the terms

of the D&O liability insurance policy issued by American Home to Onex for the period 2004-2005 or alternatively pursuant to a similar policy issued for the 2002-2003 period.

[5] The Plaintiffs also seek summary judgment against the Defendants Brit Syndicates Ltd. (Lloyd's Syndicate 2987) and Heritage Managing Agency Limited (Lloyd's Syndicate 3245), XL Insurance Company Limited, Liberty Mutual Insurance Company and Houston Casualty Company (collectively the "Excess Insurers") to pay defence costs pursuant to excess follow-form D&O liability insurance policies issued by the Excess Insurers to Onex in excess of American Home's D&O policy for the period 2004-2005.

[6] In response, each of American Home and the Excess Insurers move for summary judgment against the Plaintiffs requesting the Action be dismissed in its entirety.

[7] The Plaintiffs' claims against the remaining Defendants, Lloyd's Underwriters Syndicates No. 2623, 0623, 0033 and AIG Europe (UK) Limited, also excess insurers for the 2004-2005 D&O policy, were settled prior to the argument of the motions and the Action has been dismissed against them, on consent.

[8] On April 6, 2011, I received a letter from counsel for the Excess Insurers indicating that they had been advised by counsel for the Plaintiffs that the Kipperman Action has been settled for US \$9.25 million. A Stipulation of Dismissal was filed with the US District Court for the Northern District of Georgia on March 24, 2011. The letter requested that I postpone releasing my decision pending discussions between the parties

[9] Following that notice, I have now been advised by the parties that as a result of the settlement of the Kipperman Action, the total amount of the Plaintiffs' claim in the Action in respect of both liability and defence costs will not impact the third and fifth excess layers of D&O coverage insured by excess D&O policies issued by the Defendants Liberty Mutual Insurance Company and Houston Casualty Company respectively for the 2004-2005 period. As a result, the parties have agreed that the Action should be dismissed against Liberty Mutual Insurance Company and Houston Casualty Company on consent with the issue of costs to be dealt with following my decision on the motions.

#### The Facts

[10] The following are the material facts concerning the issues raised by the motions as found by me based upon the voluminous material submitted by the parties. I do not believe that any of the facts as I have found them are in dispute between the parties. The disputes concerning facts centre around the subjective statements of the parties and their agents about the events in issue, which I will have more to say about later.

#### Background

##### *(i) The Parties*

[11] Onex is an Ontario corporation in the business of private equity investment and asset management. Onex, by itself and with partners, regularly acquires operating businesses with a view to creating value and subsequently either retaining them or disposing of them.

Onex's directors and officers often serve in a dual capacity of officer and director of its subsidiaries while they remain officers and directors of Onex.

[12] At all material times, Schwartz, Govan, Hilson and Wright were directors and/or officers of Onex. Hilson and Wright were also directors and officers of Magnatrax.

[13] American Home (now known as Chartis Insurance Company of Canada) is an insurance company who was, at all material times, a member of the American International Group. As more particularly described herein, American Home issued a number of annual D&O liability insurance policies to Onex and one D&O policy to Magnatrax during the period 2002 – 2005.

[14] The Excess Insurers are insurers who issued excess, follow-form D&O policies of insurance to Onex in respect of the American Home D&O policy for the 2004-2005 period, as more particularly described herein.

(ii) *Non-Parties*

[15] Magnatrax was incorporated in April 1999 in Delaware by Onex. During the period from May 1999 to March 2000, Magnatrax and/or its subsidiaries purchased several American and Canadian manufacturing companies which were in the business of manufacturing and selling pre-engineered metal building and other diversified construction products and services for commercial, non-residential applications and limited residential applications. Magnatrax remained a subsidiary of Onex from the date of its incorporation until November, 2003.

[16] Aon Reed Stenhouse Inc. ("Aon") is an insurance broker who at all material times acted on behalf of Onex and Magnatrx as their agent and broker of record in respect of the insurance policies at issue in the Action. Aon is not a party to the Action.

(iii) *The Onex 2002-2003 D&O Policy*

[17] Onex, like most public companies, regularly purchased D&O liability insurance to protect both its own directors and officers and also the directors and officers of its subsidiaries from claims arising from their actions while acting in their capacity as directors and officers.

[18] Effective November 29, 2002, American Home issued to Onex, its subsidiaries and other named Onex entities, Executive and Organization Liability Insurance Policy number 240 22 88 for the period of November 29, 2002 to November 29, 2003 (the "2002-2003 D&O Policy"). The 2002-2003 D&O Policy covered officers and directors of Onex and its subsidiaries in respect of liability for claims first made against them and reported during the policy period and had an aggregate limit of liability for all loss, including defence costs, of US \$15 million.

[19] In addition to the 2002-2003 D&O Policy from American Home, Onex also obtained three excess follow-form policies from three different insurers each with a limit of US \$15 million, giving it D&O liability coverage for the period from November 29, 2002 to November 29, 2003 in the total amount of US \$60 million.

[20] The 2002-2003 D&O Policy provided that, generally, coverage applied to claims which were both made against the Insured and reported to American Home during the Policy period. The 2002-2003 D&O Policy contained the following Notice in capital letters at the beginning of the Policy:

NOTICE: COVERAGES A, B AND C ARE CLAIMS MADE. THE COVERAGE OF THIS POLICY IS GENERALLY LIMITED TO LIABILITY FOR CLAIMS THAT ARE FIRST MADE AGAINST THE INSURED AND CRISIS FIRST OCCURRING DURING THE POLICY PERIOD AND REPORTED IN WRITING TO THE INSURED PURSUANT TO THE TERMS HEREIN.

[21] The 2002-2003 D&O Policy provided for three different types of coverage. The Executive Liability portion, referred to as Coverage A, provided as follows:

#### INSURING AGREEMENTS

With respect to Coverage A, B and C, solely with respect to Claims first made against an Insured during the Policy Period or the Discovery Period (if applicable) and reported to the Insurer pursuant to the terms of this policy, and subject to the other terms, conditions and limitations of this policy, this policy affords the following coverage:

#### Coverage A: Executive Liability Insurance

This policy shall pay the Loss of any Insured Person arising from a Claim (including, but not limited to, an Employment Practices Claim, an Oppressive Conduct Claim, a Canadian Pollution Claim and a Statutory Claim) made against such Insured Person for any Wrongful Act of such Insured Person, except when and to the extent that an Organization has indemnified such Insured Person. Coverage A shall not apply to Loss arising from a Claim made against an Outside Entity Executive.

[22] The capitalized words in the above paragraphs are all defined terms contained in clause 2 of the 2002-2003 D&O Policy.

(iv) *The Magnatrax Run-Off Policy*

[23] In early January 2003, Onex was considering a sale of Magnatrax to a third party. It advised Aon and asked it to explore the possibility of obtaining a run-off D&O liability policy for Magnatrax.

[24] As noted, the 2002-2003 D&O Policy covered directors and officers of both Onex and its subsidiaries which included Magnatrax. If Magnatrax ceased to be a subsidiary of Onex, however, it and its directors and officers would no longer be covered under the 2002-2003 D&O Policy. Accordingly, in order to protect Magnatrax's directors and officers from "Claims" arising from alleged "Wrongful Acts" said to have been committed by them prior to the date Magnatrax ceased to be a subsidiary of Onex but made against them after that date, it would be necessary for Magnatrax to obtain separate coverage for its directors and officers for a term of several years until such claims could no longer be brought. Such a policy is referred to as a "run-off" policy.

[25] In response to Onex's request, Aon approached American Home for a quote for a run-off D&O liability policy for Magnatrax's directors and officers.

[26] On January 10, 2003, American Home provided Aon with a quote for an Executive and Organization Liability Insurance Policy for Magnatrax with a limit of US \$15 million for a six year run-off period. The quotation provided on page 2 thereof for a number of endorsements, including #13 - Non-Pyramiding of Limits; and #14 - Absolute Onex

Corporation Exclusion – Carve-out for co-defendant with Onex Corporation. Undemeath the listed Exclusions, the following appeared: “NOTE: Endorsements to be added to Onex Corporation Policy 1. Absolute Exclusion from Magnatrax Corporation; 2. Non-Pyramiding of Limits”.

[27] Aon had a number of concerns with American Home’s quote. In particular, it was concerned that the proposed Magnatrax run-off policy would only include coverage for Onex’s directors or officers in circumstances where they were named as co-defendants in a claim along with any Magnatrax directors and officers.

[28] Before Aon could resolve its concerns with American Home arising from the quote, Aon was advised by Onex sometime in late January 2003 that the proposed sale of Magnatrax was off. As a result, discussions between Aon and American Home concerning a Magnatrax run-off D&O liability policy ceased.

[29] Approximately five months later, on the evening of Sunday May 11, 2003, Charles Fogden, the account manager at Aon responsible for Onex, received a telephone call at his home from Hilson and other members of the Magnatrax Board of Directors advising him that Magnatrax intended to file for bankruptcy protection in the United States. Fogden was asked, on behalf of the Magnatrax Board, to arrange a primary run-off D&O policy for Magnatrax with American Home with a US \$15 million limit effective on or about May 12, 2003 in the form arranged when considering the sale earlier in January, 2003.

[30] On May 12, 2003, Fogden arranged for Aon to contact American Home as a result of which American Home issued a temporary and conditional binder of coverage for Executive and Organization Liability Policy number 350 35 03 for Magnatrx for the period from May 12, 2003 to May 12, 2009 with a limit of US \$15 million (the "Magnatrx Run-Off Policy"). On page two of American Home's binder, 13 Endorsements were listed. In particular, Endorsements #12 and #13 were: "12. Non-pyramiding of Limits (To Be Manuscripted) and 13. Absolute Onex Corporation Exclusion – Carve-put [sic] for co-defendant with Onex Corporation (To Be Manuscripted)".

[31] Underneath the Endorsements, the following wording appeared:

NOTE: Endorsements to be added to Onex Corporation Policy

1. Non-pyramiding of Limits (To Be Manuscripted)
2. Absolute Exclusion from Magnatrx Corporation (To Be Manuscripted)

[32] The words "To Be Manuscripted" meant that the wording of the endorsement to be added to the policy was to be drafted.

[33] At some point after inception of the Magnatrx Run-Off Policy, American Home provided the Policy wording to Magnatrx comprised of both the general policy wording and the specific endorsements. The general wording of the Magnatrx Run-Off Policy is identical to the wording in the 2002-2003 D&O Policy save and except for the fact that Magnatrx is the Named Entity. While some of the Endorsements are also the same, some are different. In that

regard, the Endorsements noted as #12 and #13 in the temporary and conditional binder of coverage dated May 12, 2003, appear as Endorsements #16 and #14 respectively in the Magnatrax Run-Off Policy.

[34] Endorsement #16 deals with co-ordinating the limits of liability between the Magnatrax Run-Off Policy and the 2002-2003 D&O Policy in the event of a Claim. It provides as follows:

In consideration of the premium charged, it is hereby understood and agreed that, with respect to any Claim under this policy for which coverage is provided by one or more other policies issued by the Insurer or any other member of the American International Group (AIG), (or would be provided but for the exhaustion of the limit of liability, the applicability of the retention/deductible amount or coinsurance amount, or the failure of the Insured to submit a notice of a Claim), the Limit of Liability provided by virtue of this policy shall be reduced by the limit of liability provided by said other AIG policy.

Notwithstanding the above, in the event such other AIG policy contains a provision which is similar in intent to the foregoing paragraph, then the foregoing paragraph will not apply, but instead:

- 1) the Insurer shall not be liable under this policy for a greater proportion of the Loss than the applicable Limit of Liability under this policy bears to the total limit of liability of all such policies, and
- 2) the maximum amount payable under all such policies shall not exceed the limit of liability of the policy that has the highest available limit of liability.

Nothing contained in this endorsement shall be construed to increase the limit of liability of this policy.

[35] Endorsement #4 of the Magnatrax Run-Off Policy deals with the exclusion of Onex but provides a carve-out for Onex directors and officers in certain circumstances. It provides as follows:

In consideration of the premium charged, it is hereby understood and agreed that the term "Organization" is amended to include the following entity, subject to the terms, conditions and limitations of this policy.

ENTITY

Onex Corporation

Coverage as is afforded under this policy with respect to a Claim made against Onex Corporation or any Insured Persons thereof shall only apply if: (1) such Claim relates to a Wrongful Act committed by an Insured (other than Onex Corporation or an Insured Person thereof); and (2) an Insured (other than Onex Corporation or an Insured Person thereof) is and remains a defendant in the Claim along with Onex Corporation or any Insured Person thereof.

In all events coverage as is afforded under this policy with respect to a Claim made against Onex Corporation or any Insured Person thereof shall only apply to Wrongful Acts committed or allegedly committed prior to May 12, 2003.

[36] In conjunction with the Magnatrax Run-Off Policy and as provided in the temporary and conditional binder of coverage dated May 12, 2003, American Home issued Endorsement #14 to the 2002-2003 D&O Policy effective May 12, 2003. Endorsement #14, entitled "Specific Entity/Subsidiary Exclusion", provides as follows:

In consideration of the premium charged, it is hereby understood and agreed that the Insurer shall not be liable for Loss alleging, arising out of, based upon or attributable to or in connection with any Claim brought by or made against the Entity listed below and/or any Insureds thereof.

1. MAGNATRAX Corporation (including any subsidiary or affiliate thereof)

It is further understood and agreed that the Definition of Subsidiary shall not include MAGNATRAX Corporation. Further, the Insurer shall not be liable to make any payment for Loss in connection with any Claim made against an insured alleging, arising out of, based upon or attributable to any breach of duty, act, error or omission of MAGNATRAX Corporation, or any director, officer, member of the board of managers or employee thereof.

[37] Notwithstanding the temporary and conditional binder of coverage for the Magnatrax Run-Off Policy provided that an endorsement would be added to the 2002-2003 D&O Policy in respect of the non-pyramiding of limits, no such endorsement was ever added.

[38] No excess insurance beyond the U.S. \$15 million limit provided by the Magnatrax Run-Off Policy was ever sought or obtained.

(v) *Magnatrax's Bankruptcy Proceedings*

[39] On May 12, 2003, the same day that American Home agreed to bind the Magnatrax Run-Off Policy, Magnatrax, together with 16 of its direct and indirect subsidiaries each filed a voluntary petition for reorganization under Chapter 11 of the United States Bankruptcy Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the District of Delaware.

[40] On May 22, 2003, the Office of the United States Trustee formed an official committee of unsecured creditors (the "Creditors' Committee") who in turn selected the law firm of Foley & Lardner ("Foley") to act as its counsel. Pursuant to powers under the Bankruptcy Code, the Creditors' Committee carried out a detailed investigation of various matters relating to the activities of Magnatrax and its subsidiaries including certain acquisition transactions and their financing.

[41] On August 19, 2003, the Creditors' Committee reached an agreement with, among others, Magnatrax and its subsidiaries on a Plan of Reorganization dated September 17,

2003 (the "Magnatrx Plan of Reorganization") which was subsequently confirmed by the U.S. Bankruptcy Court on November 17, 2003. As a result of the U.S. Bankruptcy Court approval of the Magnatrx Plan of Reorganization, Onex ceased to have any ownership interest in Magnatrx at that time.

[42] On January 20, 2004, Magnatrx emerged from Chapter 11 protection.

(vi) *The Foley Letter*

[43] By letter dated August 1, 2003, Foley wrote to counsel for Magnatrx on behalf of the Creditors' Committee (the "Foley Letter"), stating that it believed Magnatrx and its subsidiaries had various causes of action against, among others, Onex, its affiliates and officers and directors. The Foley Letter states, in part:

..... the [Creditors'] Committee believes that [Magnatrx and its subsidiaries] have various claims against parties involved in the May 1999, September 1999, and March 2000 transactions, as well as the credit facilities and related agreements supporting those transactions. More specifically, the [Creditors'] Committee asserts that numerous claims finding their genesis in fraudulent transfers, breach of fiduciary duty, aiding and abetting both breach of fiduciary duty and fraudulent transfers, equitable subordination, unjust enrichment, declaratory relief, preference actions, and possibly other claims yet to be identified, should all be pursued.

[44] The Foley Letter goes on to list a number of entities and individuals against whom some or all of the claims should be pursued, and specifically refers to Onex and its officers and directors.

[45] The Foley Letter concludes by requesting Magnatrax's "immediate confirmation" that Magnatrax and its subsidiaries will prosecute the listed claims against all of the individuals and entities noted and if they did not intend to do so, to provide immediate confirmation so that the Creditors Committee could then do so on their behalf.

[46] On August 7, 2003, Magnatrax's counsel forwarded the Foley Letter to Mr. Fogden at Aon by email inquiring as to what notice should be sent to insurers on behalf of Magnatrax and its officers and directors. Mr. Fogden replied by email on August 8, 2003 that they would put American Home on notice.

[47] On November 28, 2003, the day before the 2002-2003 D&O Policy expired, Aon faxed the Foley Letter to American Home. The fax covering page references the Magnatrax Run-Off Policy in the reference line at the outset and states:

Enclosed is a letter of August 1, 2003 from Foley & Lardner, Attorneys at Law, which contains information on a situation which could in future give rise to a claim under the above mentioned policy.  
Under separate cover we are also reporting this issue under a Directors & Officers policy for Onex Corporation which is also written through your office.

[48] Also on November 28, 2003, Aon sent a similar fax to American Home in respect of the 2002-2003 D&O Policy.

[49] American Home subsequently acknowledged receipt of the Aon claims letters and advised that it was setting up claim files for both the 2002-2003 D&O Policy and the

Magnatrx Run-Off Policy to enable a "full assessment of coverage" to be made. American Home reserved its rights, privileges and defences under the Policies.

[50] Having heard nothing further about the claim for more than a year from the initial notice, American Home wrote to Aon in December 2004, asking if there still existed a threat of a "Claim" and indicating that in the absence of further developments, American Home intended to close its files in 60 days. American Home once again reserved all rights under both the 2002-2003 D&O Policy and the Magnatrx Run-Off Policy. In the absence of any further information from either Magnatrx or Onex concerning the information in the Foley Letter, American Home closed its claim files on March 16, 2005.

*(vii) The Onex 2003-2004 D&O Policy*

[51] In the fall of 2003, American Home renewed the 2002-2003 D&O Policy by issuing Executive and Organization Liability Insurance Policy No. 378 16 65 to Onex with primary limits of US \$15 million for the period from November 29, 2003 to November 29, 2004 (the "2003-2004 D&O Policy").

[52] The 2003-2004 D&O Policy was very similar to the wording of the 2002-2003 D&O Policy. The general policy wording was identical. The wording of the endorsements was for the most part similar although there were some differences. In particular, Endorsement 13 provided a Specific Entity Exclusion for claims involving Magnatrx which had the identical wording of the Specific Entity Exclusion found in the 2002-2003 D&O Policy at Endorsement 14.

[53] In addition to the 2003-2004 D&O Policy, Onex again obtained excess directors and officers insurance for the same period.

*(viii) The Onex 2004-2005 D&O Policy*

[54] In the fall of 2004, Aon, on behalf of Onex, once again solicited renewals for Onex's D&O liability insurance program for the 2004 - 2005 period.

[55] On November 11, 2004, American Home provided Aon with a quote to renew the 2003-2004 Onex Policy on the basis of an aggregate limit of liability of US \$15 million for the period from November 29, 2004 to November 29, 2005 (the "Quote"). The Quote identified a number of endorsements that would be included in the Onex D&O Policy once issued. Amongst the endorsements listed was a Specific Entity Exclusion for Magnatrax.

[56] On November 25, 2004, American Home issued its temporary and conditional binder of insurance coverage for D&O liability policy 358 12 14 for the period from November 29, 2004 to November 29, 2005 on the basis of an aggregate limit of liability of US \$15 million (the "2004-2005 D&O Policy") as had been previously set out in the Quote (the "Binder"). The Binder provided a list of twenty endorsements which would be included in the Policy, including Endorsement #13, a Specific Entity Exclusion for Magnatrax.

[57] In order to obtain excess D&O liability insurance for Onex over and above the limits of the 2004-2005 D&O Policy from American Home, Aon provided the Excess Insurers with a Directors' and Officers' Liability Insurance renewal application form containing

information about Onex's company background and its performance over the last policy period, along with the Quote and the Binder.

[58] Based on this information, each of the Excess Insurers agreed to provide "follow form" coverage to the 2004-2005 D&O Policy, thereby incorporating into each excess layer the terms and conditions set out in the 2004-2005 D&O Policy. The excess insurance over and above the US \$15 million provided by the 2004-2005 D&O Policy totalled US\$75 million.

[59] In particular, the Excess Insurers provided the following coverage:

- (a) The First Excess Insurer, Brit Syndicates Ltd. (Lloyd's Syndicate 2987) and Heritage Managing Agency Limited (Lloyd's Syndicated 3245), provided its binder for the First Excess Layer on November 29, 2004 offering coverage on the basis of limits of liability of US\$20 million in excess of \$15 million provided to Onex by American Home pursuant to the 2004-2005 D&O Policy;
- (b) The Second Excess Insurer, XL Company Limited, provided its binder for the Second Excess Layer on November 29, 2004 offering coverage on the basis of limits of liability of US\$20 million in excess of the US \$35 million provided to Onex by American Home and the Excess Insurers pursuant to the 2004-2005 D&O Policy;
- (c) The Third Excess Insurer, Liberty Mutual Insurance Company, provided its binder on the Third Excess Layer on December 7, 2004 on the basis of liability of US\$20 million in excess of the US\$55 million provided to Onex by American Home and the Excess Insurers pursuant to the 2004-2005 D&O Policy; and
- (d) The Fifth Excess Insurer, Houston Casualty Company, provided its binder on the Fifth Excess Layer on December 1, 2004 offering on the basis of limits of liability of US\$5 million in excess of the US \$85 million provided to Onex by American Home and the Excess Insurers pursuant to the 2004-2005 D&O Policy.

(Collectively the "Excess Policies")

[60] The policy wording for the 2004-2005 D&O Policy was not sent to Aon for its review until May 10, 2005. Following its receipt, discussions took place between Aon and American Home concerning the wording of some of the endorsements. In particular, Aon took the position that proposed Endorsement #13, which was the Specific Entity/Subsidiary Exclusion in respect of Magnatrax which had been present as Endorsement #14 in the 2002-2003 D&O Policy and Endorsement #13 in the 2003-2004 D&O Policy should be changed to a Prior Acts Exclusion to provide coverage for Magnatrax officers and directors for the period May 12, 2003 to January 20, 2004, which was the time Magnatrax and its subsidiaries were in Chapter 11. American Home agreed and on July 5, 2005, it sent Aon Endorsement #23 entitled Prior Acts Exclusion For Listed Entities which became part of the 2004-2005 D&O Policy.

[61] Endorsement #23 of the 2004-2005 D&O Policy provides:

In consideration of the premium charged, it is hereby understood and agreed that the term Subsidiary is amended to include the entity(ies) listed below, but only for Wrongful Acts committed by such entity(ies) and/or any Insureds thereof which occurred subsequent to such entity's respective acquisition/creation date listed below and prior to the time the Named Entity no longer maintains Management Control of such entity(ies), respectively, either directly or indirectly through one or more other Subsidiaries. Loss arising from the same or related Wrongful Act shall be deemed to arise from the first such same or related Wrongful Act.

ENTITY(IES) ACQUISITION/CREATION DATE

1. MAGNATRAX Corporation [...] May 12, 2003

For the purpose of the applicability of the coverage provided by this endorsement, the entities listed above and the Organization will be conclusively deemed to have indemnified the Insureds of [...] each respective entity to the

extent that such entity or the Organization is permitted or required to indemnify such Insureds pursuant to law or contract or the charter, bylaws, operating agreement or similar documents of an Organization. The entity and the Organization hereby agree to indemnify the Insureds to the fullest extent permitted by law, including the making in good faith of any required application for court approval.

[62] The policy wording for the 2004-2005 D&O Policy was provided by Aon to the Excess Insurers for the first time on July 13, 2005. The Excess Insurers did not agree to the wording changes agreed to between Aon and American Home subsequent to providing their binders of coverage. In particular, they did not agree to Endorsement #23.

*(ix) The Kipperman Action*

[63] Section 4.21 of the Magnatrx Plan of Reorganization provides, among other things, for the establishment of a Litigation Trust and the transfer and assignment by Magnatrx and its subsidiaries of all right, title or interest of Magnatrx and its subsidiaries in and to the "Assigned Causes of Action" to the Litigation Trust. Section 1.20 defines "Assigned Causes of Action" to mean all right, title and interest of Magnatrx and its subsidiaries "to pursue, litigate, settle or otherwise resolve any Cause of Action against Onex Corporation or any Onex Affiliate". Section 1.110 defines "Onex Affiliate" to include a number of Onex's related companies and any person who possesses the power, directly or indirectly, to direct or cause the direction of the management and policies of Onex or its related companies.

[64] As noted at the outset, the Kipperman Action was commenced on May 10, 2005 by Kipperman in his capacity as Trustee of the Magnatrx Litigation Trust.

[65] The Complaint in the Kipperman Action is 70 pages in length and asserts 19 causes of action against Onex and certain of its subsidiaries and affiliates and Schwartz, Govan, Wright and Hilson. Also named are Robert C. Blackmon Jr. and Robert T. Ammerman who were directors and officers of Magnatrax.

[66] The Complaint alleges that defendants in the Kipperman Action, including the individual Plaintiffs:

- (a) incorporated Magnatrax as a vehicle for highly leveraged acquisitions of several American and Canadian manufacturing companies, which occurred from May 1999 to March 2000;
- (b) along with affiliates, seized control of Magnatrax and its subsidiaries by a self-dealing management agreement, placing Onex personnel on boards of and in key management positions with Magnatrax entities;
- (c) used that control to obtain millions of dollars for themselves while imposing significant debt on Magnatrax entities, forcing Magnatrax into bankruptcy in May 2003 from which it emerged in late 2003, leaving hundreds of millions in pre-bankruptcy unpaid debt discharged;
- (d) through the co-defendants' conduct, left the Magnatrax entities insolvent, inadequately capitalized and unable to pay debts while millions of dollars were diverted to the defendants.

[67] Of the 19 claims asserted in the Kipperman Action, four are asserted against the individual Plaintiffs: i) breach of fiduciary duty (Count X); ii) aiding and abetting breach of fiduciary duty (Count XI); iii) civil conspiracy (Count XII); and unjust enrichment (Count XIX). Swartz, Govan, Hilson are included in the term "Management Defendants" in the Complaint.

[68] Paragraph 107 of the Complaint pleads that Onex was the *de facto* board and alter ego of Magnatrax and its subsidiaries and "Swartz and Govan were *de facto* members of the boards of Magnatrax and each of them owed the acquired companies and their creditors' fiduciary duties of care and loyalty which they breached."

[69] Count X which deals with breach of fiduciary duty alleges, in part, that Swartz and Govan "directed and controlled all of Onex's conduct under the Management Agreement and other conduct by which Onex controlled the Magnatrax entities" therefore assuming the role of *de facto* board members of all Magnatrax entities (para. 198). Paragraph 200 pleads that while acting at the behest of and beholden to Onex, the Management Defendants breached their fiduciary duties to Magnatrax and its subsidiaries. A number of examples are pleaded. Paragraphs 212 to 214 plead that Hilson, Wright, Govan and Schwartz had conflicts of interest while acting as a director/officer of Onex and a director/officer of Magnatrax or a *de facto* director.

[70] Count XI deals with the claim of aiding and abetting breach of fiduciary duty. Paragraph 218 pleads that Schwartz knowingly induced, participated and substantially assisted

in the breaches of fiduciary duty by Govan, Hilson, Wright and others. The same allegation is pleaded against Govan, Hilson and Wright in paragraphs 219 to 221 of the Complaint.

[71] Count XII which deals with the allegation of civil conspiracy is somewhat sparse. It alleges that all defendants wilfully conspired to embark on a scheme to divert value from Magnatrax to themselves (para. 226); to fraudulently transfer assets from Magnatrax to the benefit of themselves (para. 227); and to breach fiduciary duties (para. 228).

[72] Count XIX alleges unjust enrichment. Paragraph 283 pleads that as a result of complete domination and control and breaches of fiduciary duties, the defendants received a benefit from their management of the Magnatrax entities.

(x) *Notice to American Home of the Kipperman Action*

[73] On July 4, 2005, Aon, on behalf of Onex, sent a copy of the Complaint in the Kipperman Action to American Home and stated that it was notice of a Claim under the 2004-2005 D&O Policy.

[74] By letter dated September 15, 2005, American Home denied coverage of the Kipperman Action under the 2004-2005 D&O Policy on the basis that:

- (i) the allegations in the Kipperman Action all pre-date May 12, 2003 and are therefore outside the scope of coverage;

(ii) the claim is excluded as the allegations in the Kipperman Action relate to the individual Plaintiffs' actions in respect of Magnatrax and are not claims made against the individual Plaintiffs in their capacities as directors and officers of Onex; and

(iii) the allegations in the Kipperman Action involve intentional acts which are outside the scope of the 2004-2005 D&O Policy.

[75] Although American Home also initially denied coverage for the Kipperman Action under the Magnatrax Run-Off Policy, on August 28, 2006, its counsel sent a letter to counsel for the Plaintiffs indicating that, based on further review, American Home determined that the Magnatrax Run-Off Policy did provide coverage to Schwartz, Govan, Hilson and Wright as well as Messrs. Ammerman and Blackmon.

[76] American Home subsequently paid US \$1,118,008.10 to Messrs. Ammerman and Blackmon and US \$13,881,991.90 to the Plaintiffs in respect of defence costs incurred in the Kipperman Action pursuant to the Magnatrax Run-Off Policy. The total amount of US \$15 million paid by American Home is the limit of its liability pursuant to the Magnatrax Run-Off Policy.

Positions of the Parties

(a) The Plaintiffs

[77] The Plaintiffs submit that Schwartz, Govan, Hilson and Wright, in their capacity as directors and/or officers of Onex are entitled to coverage for the Kipperman Action pursuant to a D&O Policy issued by American Home. In that regard they submit that the Kipperman Action is a "Claim" made and reported during the period of the 2004-2005 D&O Policy and is therefore covered by that Policy. Accordingly, American Home and the Excess Insurers are required to indemnify the individual Plaintiffs' for their "Loss" arising from the Kipperman Action, and in particular defence costs incurred, pursuant to the terms of the 2004-2005 D&O Policy and the Excess Policies.

[78] The Plaintiffs take issue with the Defendants' position that the Foley Letter constitutes notice of circumstances in accordance with the terms of the 2002-2003 D&O Policy such that the Kipperman Action constitutes a "Claim" made during the period of that Policy. In the alternative, if the 2002-2003 D&O Policy applies, the Plaintiffs submit that American Home is required to indemnify the individual Plaintiffs' in accordance with the terms and to the limits of liability of that Policy. The Plaintiffs assert no claim against the 2002-2003 D&O Policy's excess insurers nor are they parties to the action.

[79] The Plaintiffs further submit that the payment by American Home of the US \$15 million pursuant to the provisions of the Magnatrax Run-Off Policy does not impact upon or

reduce American Home's liability either under the 2004-2005 D&O Policy or the 2002-2003 D&O Policy.

(b) American Home

[80] American Home's position is that coverage for the Kipperman Action is only available under the Magnatrax Run-Off Policy and it has paid the full extent of its liability under that Policy to the Plaintiffs.

[81] To the extent that the Kipperman Action constitutes a Claim for a Wrongful Act of an Insured under the terms of either the 2002-2003 D&O Policy or the 2004-2005 D&O Policy, American Home submits that the Foley Letter constitutes sufficient notice of circumstances within the period of the 2002-2003 D&O Policy that it is that Policy which applies to the Kipperman Action. American Home further submits, however, that based on the terms of the 2002-2003 D&O Policy and specifically Endorsement #14, the Specific Entity/Subsidiary Exclusion for Magnatrax, there is no coverage under the 2002-2003 D&O Policy in respect of the Kipperman Action.

[82] Finally, American Home submits that there is no coverage for the Kipperman Action pursuant to the 2004-2005 D&O Policy having regard to Exclusion 4(d) which specifically excludes coverage for previously reported claims.

(c) Excess Insurers

[83] The Excess Insurers join in American Home's submission that the Kipperman Action is a Claim first made and reported during the 2002-2003 D&O Policy period and therefore the Kipperman Action is a pre-existing claim which is excluded from coverage under the 2004-2005 D&O Policy by Exclusion 4(d) of the latter Policy.

[84] In the alternative, the Excess Insurers submit that if the 2004-2005 D&O Policy applies, coverage by the Excess Insurers under that Policy is excluded in accordance with the terms of Endorsement #13, the Specific Entity/Subsidiary Exclusion in respect of Magnatrx, which the Excess Insurers submit remained a term of the Excess Policies. The Excess Insurers further submit that the allegations in the Kipperman Action do not trigger coverage under the 2004-2005 D&O Policy.

[85] Finally, the Excess Insurers submit that in the event that the Court does not accept their arguments that there is no coverage under the 2004-2005 D&O Policy, the Excess Insurers submit the Plaintiffs' summary judgment motion cannot succeed as there remain genuine issues between the parties requiring a trial.

The Issues

[86] Given the positions of the parties, the following are the issues that must be determined on these motions:

1. Is summary judgment appropriate for these motions?

2. Are the defence costs incurred by the individual Plaintiffs in the Kipperman Action covered by the terms of the 2002-2003 D&O Policy and the 2004-2005 D&O Policy?
3. If the answer to 2 is yes, which Policy applies in respect of the Kipperman Action, the 2002-2003 D&O Policy or the 2004-2005 D&O Policy?
4. Depending on which Policy applies, do the exclusions or limitations of that Policy exclude coverage of Loss arising from the Kipperman Action?

#### Principles of Insurance Contract Interpretation

[87] The issues raised by the parties require the court to interpret and give reasonable meaning to the provisions of the 2002-2003 D&O Policy, the 2004-2005 D&O Policy and the Magnatrax Run-Off Policy.

[88] The principles of insurance contract interpretation have been developed and discussed by Canadian Courts at some length for many years. Most recently, they were summarized by Rothstein J. in *Progressive Homes Ltd. v. Lombard General Insurance Co. of Canada*, [2010] 2 S.C.R. 245 (S.C.C.) at paras. 21-24 as follows:

21 Principles of insurance policy interpretation have been canvassed by this Court many times and I do not intend to give a comprehensive review here (see, e.g., *Gibbens v. Co-operators Life Insurance Co.*, 2009 SCC 59, [2009] 3 S.C.R. 605 (S.C.C.), at paras. 20-28; *Jesuit Fathers*, at paras. 27-30; *Scalera*, at paras. 67-71; *Brissette v. Westbury Life Insurance Co.*, [1992] 3 S.C.R. 87 (S.C.C.), at pp. 92-93; *Consolidated-Bathurst Export Ltd. c. Mutual Boiler & Machinery Insurance Co.* (1979), [1980] 1 S.C.R. 888 (S.C.C.), at pp. 899-902). However, a brief review of the relevant principles may be a useful introduction to the interpretation of the CGL policies that follow.

22 The primary interpretive principle is that when the language of the policy is unambiguous, the court should give effect to clear language, reading the contract as a whole (Scalera, at para. 71).

23 Where the language of the insurance policy is ambiguous, the courts rely on general rules of contract construction (Consolidated-Bathurst, at pp. 900-902). For example, courts should prefer interpretations that are consistent with the reasonable expectations of the parties (Gibbens, at para. 26; Scalera, at para. 71; Consolidated-Bathurst, at p. 901), so long as such an interpretation can be supported by the text of the policy. Courts should avoid interpretations that would give rise to an unrealistic result or that would not have been in the contemplation of the parties at the time the policy was concluded (Scalera, at para. 71; Consolidated-Bathurst, at p. 901). Courts should also strive to ensure that similar insurance policies are construed consistently (Gibbens, at para. 27). These rules of construction are applied to resolve ambiguity. They do not operate to create ambiguity where there is none in the first place.

24 When these rules of construction fail to resolve the ambiguity, courts will construe the policy *contra proferentem* — against the insurer (Gibbens, at para. 25; Scalera, at para. 70; Consolidated-Bathurst, at pp. 899-901). One corollary of the *contra proferentem* rule is that coverage provisions are interpreted broadly, and exclusion clauses narrowly (Jesuit Fathers, at para. 28).

[89] The application of the above principles to the task of interpreting an insurance contract was summarized by Cronk J.A. in *Lombard Canada Ltd. v. Zurich Insurance Co.* (2010), 101 O.R. (3d) 371 (C.A.) at paras. 32-34 as follows:

32 The foundation for the relevant principles and process for the interpretation of an insurance contract is *Consolidated Bathurst Export Ltd. v. Mutual Boiler & Machinery Insurance Co.*, [1980] 1 S.C.R. 888. At pp. 899 - 901 of that case, Estey J., writing for the majority, explains the two phases of the analysis for the interpretation of any contract, including an insurance contract.

33 The first is the interpretive phase based on the guidelines for construction. Subjective intention is irrelevant at this stage of the process, although the words used may be "possibly read in light of the

surrounding circumstances which were prevalent at the time": see *Eli Lilly*, at para. 54. If the meaning is plain on the face of the contract, it is unnecessary to proceed further: see *Non-Marine Underwriters, Lloyd's of London v. Scalera*, [2000] 1 S.C.R. 551, at para. 71. However, if the interpretive phase results in two equally reasonable interpretations, the contract is ambiguous. In those circumstances, the court turns to the second phase of the inquiry. At this phase, the court may consider extrinsic evidence: see *Eli Lilly*, at para. 55. As well, the court may consider the applicability of *contra proferentem*: see *Consolidated Bathurst*, at p. 901.

34 In the interpretive phase, the onus is upon the insured to show that the loss is covered by the policy in question. Once the insured has done so, the burden shifts to the insurer to show otherwise, including by reason of the operation of an exclusion or limitation in the insurance contract: see *Continental Insurance Co. v. Dalton Cartage Co.*, [1982] 1 S.C.R. 164; *Canadian National Railway Co. v. Royal and Sun Alliance Insurance Co. of Canada*, [2008] 2 S.C.R. 453, at para. 34; *Co-Operators Life Insurance Co. v. Gibbens*, [2009] 3 S.C.R. 605, at para. 51; Denis Boivin, *Insurance Law* (Irwin Toronto: Irwin Law, 2004) at p. 190. In interpreting a provision, the court will also recognize that coverage provisions are "construed broadly and exclusion clauses narrowly": see *Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co.*, [1993] 1 S.C.R. 252, at p. 269; *Scalera*, at para. 70.

#### Claims Made Liability Insurance Policies

[90] In *Reid Crowther & Partners Ltd. v. Simcoe & Erie General Insurance Co.*, [1993] 1 S.C.R. 252 (S.C.C.), the Supreme Court discussed "claims made" liability insurance policies. The Court points out, at para. 14 of the decision, that when considering a "claims-made" policy, it is important to examine the particular wording of the policy in issue as a whole to determine the nature of the policy and how coverage applies.

### Summary Judgment

[91] Prior to embarking on the interpretation of the Policies as they relate to the issues between the parties, I want to address at the outset the Excess Insurers submission that, in the event that the court rejects their defences, the Plaintiff's motion for summary judgment cannot succeed because there are genuine issues which require a trial.

[92] As noted, the Excess Insurers submit that their motion for summary judgment, which is premised on their defences to the Plaintiffs' claim being successful, should be allowed. In the event, however, that their defences are not accepted by the Court, the Excess Insurers submit that the Plaintiffs' motion for summary judgment cannot succeed because there are genuine issues which require a trial.

[93] Rule 20.04 provides that the Court shall grant summary judgment if it is satisfied that there is no genuine issue requiring a trial. While the Rule now specifically permits the motions judge to weigh the evidence presented on the motion, evaluate the credibility of a deponent and draw reasonable inferences from the evidence, it does not eliminate a trial in circumstances where interests of justice require that the issues be resolved, not on the motion record, but rather with viva voce evidence. Depending on the issue to be decided, this may be accomplished either as part of the summary judgment motion itself by ordering oral evidence (Rule 20.04(2.2)) or by requiring a full trial. See: *New Solutions Extrusion Corp. v. Gauthier*, [2010] O.J. No. 661 (S.C.J.); *Canadian Premier Life Insurance Co. v. Sears Canada Inc.*, [2010] O.J. No. 3987 (S.C.J.).

[94] I agree with the guiding principles for Rule 20 as set forth by Pepall J. in *Canadian Premier Life Insurance*, supra, at para. 70:

- The court must be satisfied that there is no genuine issue requiring a trial.
- To be satisfied, the court may weigh the evidence, evaluate the credibility of a deponent, draw any reasonable inference from the evidence, and order that oral evidence be presented. By implication, these powers may involve the making of factual findings including a finding of a material fact.
- The motions judge should take a hard look at all of the evidence to determine whether there is a genuine issue requiring a trial.
- The burden of proof to establish that there is no genuine issue requiring a trial is on the moving party.
- The respondent may not rest solely on the allegations or denials in its pleading.
- Each side should put its best foot forward.
- The Rule should be interpreted broadly so as to achieve the objectives of reduction of delay and costs, access to justice, and flexibility. At the same time, it must be acknowledged that elimination of trials is not an objective. At its core, justice is the ultimate objective. It is not to be sacrificed in the interests of speed and economy. That said, Rule 20 clearly contemplates that justice, speed and economy are not mutually exclusive attributes.

[95] The purpose of summary judgment is to finally dispose of non-complex cases in a summary cost effective manner. That does not mean that summary judgment is restricted or should be restricted to smaller cases. Actions where the motion has an extensive evidentiary record can also be subject to summary judgment. In such circumstances, however, the court

must be particularly vigilant in ensuring that the issues can be decided on the record without the safeguards provided by a trial. See: *Canadian Premier Life Insurance*, supra, at para. 71.

[96] The record in this case is comprised of nine volumes. In addition to the D&O Policies in issue, it contains 16 affidavits, transcripts of extensive cross-examinations and numerous documents.

[97] The facts as I have recited them, although lengthy and somewhat complex, are not, in the final analysis, in dispute between the parties. They serve to set out the factual matrix of the D&O Policies in issue. What is in dispute factually are the various assertions of intention by the various parties. In my view it is not necessary to resolve any of those factual disputes to resolve the motions. As will become apparent from my reasons that follow, such evidence is not admissible given my view that the provisions of the D&O Policies in issue are clear and unambiguous.

[98] Accordingly, notwithstanding that the Record in this case is extremely large, I am satisfied that all of the issues between the parties as raised in the Plaintiffs' motion and the Defendants' cross-motions can be determined by way of summary judgment.

Are the defence costs incurred by the individual Plaintiffs in the Kipperman Action covered by the 2002-2003 D&O Policy and the 2004-2005 D&O Policy?

[99] As noted in *Lombard Canada v. Zurich Insurance*, supra, at para. 34, the onus is on the Plaintiffs to establish that their defence costs are covered by either the 2004-2005 D&O

Policy or the 2002-2003 D&O Policy. In order to determine whether the Plaintiffs have met their onus, it is necessary to consider two questions: first, whether the Claims asserted against the Individual Plaintiffs in the Kipperman Action are covered under the Onex D&O Policies and second, whether the Plaintiffs are entitled to payment of their defence costs in advance of a final determination in the Kipperman Action.

- a) Do the allegations in the Kipperman Action constitute a Claim against an Insured Person for a Wrongful Act as those terms are defined in both the 2002-2003 Onex Policy and the 2004-2005 Onex Policy?

[100] The basic coverage wording in each of the 2002-2003 D&O Policy, the 2004-2005 D&O Policy and the Magnatrx Run-Off Policy is identical. Coverage A, which is Executive Liability, requires American Home to pay the "Loss" arising from a "Claim" made against an "Insured Person" alleging a "Wrongful Act" by such Insured Person.

[101] Clause 2 of the Policies sets out the definitions and defines Claim as follows:

(c) "Claim" means:

- (1) a written demand for monetary, non-monetary or injunctive relief;
- (2) a civil, criminal, administrative, regulatory or arbitration proceeding for monetary, non-monetary or injunctive relief which is commenced by: (i) service of a Writ of Summons, Statement of Claim or similar originating legal document; (ii) return of a summons, information, indictment or similar document (in the case of a criminal proceeding); or (iii) receipt or filing of a

notice of charges; or

(3) a civil, criminal, administrative or regulatory investigation of an Insured

Person:

- (i) once such Insured Person is identified in writing by such investigating authority as a person against whom a proceeding described in Definition (c) (2) may be commenced; or
- (ii) in the case of an investigation by any PSC or similar foreign securities authority, after the service of a subpoena upon such Insured Person.

The term "Claim" shall include any Securities Claim, Employment Practices Claim, Oppressive Conduct Claim, Canadian Pollution Claim and Statutory Claim.

[102] It is clear in my view that the Kipperman Action constitutes a "Claim" as that term is defined in the Policies. It is a civil proceeding commenced by Complaint which is an originating legal document in the United States District Court as provided in clause 2(c)(2) of the above definition.

[103] Clause 2 of the Policies further provides:

(q) "Insured Person" means any:

- (1) Executive of an Organization;
- (2) Employee of an Organization; or
- (3) Outside Entity Executive.

(l) "Executive" means any:

- (1) past, present and future duly elected or appointed director, officer, trustee or governor of a corporation, management committee member of a joint venture and member of the management board of a limited liability company (or equivalent position), including a de facto director, officer, trustee,

governor, management committee member or member of the management board of such entities;

- (w) "Organization" means:
- (1) the Named Entity;
  - (2) each Subsidiary; and
  - (3) in the event of a bankruptcy proceeding shall be instituted by or against the foregoing entities in the United States the resulting debtor-in-possession (or equivalent status outside the United States), if any.

[104] As Onex is a Named Entity in both the 2002-2003 D&O Policy and the 2004-2005 D&O Policy, it is an "Organization" as defined in clause 2(w)(1) of those Policies and Schwartz, Govan, Hilson and Wright, as directors and/or officers of Onex, are each "Insured Persons" as defined by clause 2(q)(1) of those Policies.

[105] Further, based on a review of the entire Complaint in the Kipperman Action and in particular the allegations against Schwartz, Govan, Hilson and Wright, it is my view that the claims against the individual Plaintiffs are asserted against them in their capacity both as directors and officers of Onex and as directors (or de facto directors in the case of Schwartz and Govan) and officers of Magnatrax. The overarching theme of the Complaint is that Onex, as directed by the individual Plaintiffs in their capacity as Onex directors and officers, engineered the demise of Magnatrax and its subsidiaries for their collective benefit. In that regard, the claims of aiding and abetting breach of fiduciary duty, civil conspiracy and unjust enrichment particularly relate to activities of Schwartz, Govan, Hilson and Wright in their capacity as directors and officers of Onex.

[106] “Wrongful Act” is defined in clause 2(ee) as follows:

(ee) “Wrongful Act” means:

- (1) any actual or alleged breach of duty, neglect, error, misstatement, misleading statement, omission or act or any actual or alleged Employment Practices Violation:
  - (i) with respect to any Executive of an Organization, by such Executive in his or her capacity as such or any matter claimed against such Executive solely by reason of his or her status as such;
  - (ii) with respect to any Executive of an Organization, by such Employee in his or her capacity as such, but solely in regard to any: (a) Securities Claim; or (b) other Claim so long as such other Claim is also made and continuously maintained against an Executive of an Organization; or
  - (iii) with respect to any Outside Entity Executive, by such Outside Entity Executive solely by reason of his or her status as such;

[107] In my view, the claims asserted in the Kipperman Action against Schwartz, Govan, Hilson and Wright acting in their capacity as directors and/or officers of Onex, constitute a “Wrongful Act” as defined in clause 2(ee) of the Policies. The claims involve alleged acts by the individual Plaintiffs in their capacity as directors and officers of Onex.

[108] The Excess Insurers submit that the claims in the Kipperman Action involve intentional acts which are outside the scope of coverage of the Policies. As noted, “Wrongful Act” includes “any actual or alleged breach of duty, neglect, error, misstatement, misleading statement, omission or act....” A “Claim” includes a criminal proceeding or investigation, any Securities Claim, Employment Practice Claim, and Oppressive Conduct Claim. While the provisions of the Policies exclude certain specific acts such as deliberate criminal or fraudulent acts, it is clear in my view from the definition of “Wrongful Acts” in the Policies that, subject to

the listed exclusions which are not applicable in respect of the claims asserted here, the Policies provide coverage in respect of intentional acts.

[109] In its counsel's letter of August 28, 2006 agreeing that the claims against Schwartz, Govan, Hilson and Wright in the Kipperman Action were covered under the Magnatrax Run-Off Policy, American Home conceded that such claims would be afforded coverage as Insured Persons of Onex by virtue of Endorsement #4 to the Magnatrax Run-Off Policy so long as an Insured other than Onex or an Insured Person thereof remains a defendant in the Kipperman Action. Implicit in this concession, in my view, is that the claims alleged in the Kipperman Action constitute a "Wrongful Act" within the meaning of the Policy. As noted, the material wording in respect of coverage in the Magnatrax Run-Off Policy is identical to the wording in each of the 2002-2003 D&O Policy and the 2004-2005 D&O Policy.

[110] Accordingly, I am of the view that the Plaintiffs have met their onus. Based on the plain wording of the Policies, the claims asserted against Schwartz, Govan, Hilson and Wright in the Kipperman Action are Claims made against Insured Persons for Wrongful Acts as those terms are defined in the Policies and therefore fall within Coverage A, the basic coverage section of each of the Policies.

b) Are the Plaintiffs are entitled to payment of their defence costs in advance of a final determination in the Kipperman Action?

[111] Both the 2002-2003 D&O Policy and the 2004-2005 D&O Policy define "Loss" in clause 2(r) to include Defence Costs which is further defined to mean reasonable and

necessary fees, costs and expenses consented to by the Insurer resulting solely from the investigation, adjustment, defence and/or appeal of a Claim against an Insured.

[112] Clause 2(r) of the Policies defines "Loss" as follows:

(r) "Loss" means damages (including aggravated damages), settlements, judgments (including pre/post-judgment interest on a covered judgment), Defence Costs and Crisis Loss; however, "Loss" (other than Defence Costs) shall not include: (1) civil or criminal fines or penalties; (2) taxes; (3) punitive or exemplary damages; (4) multiplied portion of multiplied damages; (5) any amounts for which an Insured is not financially liable or which are without legal recourse to an Insured; and (6) matters which may be deemed uninsurable under the provincial or state law pursuant to which this policy shall be construed.

[113] Clause 2(h) further defines "Defence Costs" as follows:

(h) "Defence Costs" means reasonable and necessary fees, costs and expenses consented to by the Insurer (including premiums for any appeal bond, attachment bond or similar bond arising out of a covered judgment, but without any obligation to apply for or furnish any such bond) resulting solely from the investigation, adjustment, defence and/or appeal of a Claim against an Insured, but excluding any compensation of any Insured Person or any Employee of an Organization.

[114] The Policies have the following Notice at the beginning of each of the Policies wordings:

NOTICE: THE INSURER DOES NOT ASSUME ANY DUTY TO DEFEND. THE INSURER MUST ADVANCE DEFENCE COSTS, EXCESS OF THE APPLICABLE RETENTION, PURSUANT TO THE TERMS HEREIN PRIOR TO THE FINAL DISPOSITION OF THE CLAIM.

[115] Clause 8 in each of the Policies, as set forth in Endorsement #11 in each of the Policies, provides in part, as follows:

8. DEFENCE COSTS, SETTLEMENTS, JUDGMENTS (INCLUDING THE ADVANCEMENT OF DEFENCE COSTS)

- (a) Under Coverage A,B and C of this policy, except as hereinafter stated, the Insurer shall advance, excess of any applicable retention amount, covered Defence Costs no later than ninety (90) days after the receipt by the Insurer of such defence bills. Such advance payments by the Insurer shall be repaid to the Insurer by each and every Insured Person or Organization, severally according to their respective interests, in the event and to the extent that any such Insured Person or Organization shall not be entitled under this policy to payment of such Loss.
- (b) The Insurer does not, under this policy assume a duty to defend. The Insureds [sic] Person and, with respect to Coverage B, the Organization, shall defend and contest any Claim made against them. ....

[116] In my view, the above wording of the Policies is clear and unambiguous. The Insurer, American Home and the Excess Insurers, have a duty to advance defence costs prior to the final disposition of the Kipperman Action.

[117] The Plaintiffs submit that the principles developed by the courts in the duty to defend cases provide useful guidance in determining when the obligation to advance pay defence costs arises. The duty to defend cases impose a duty to defend on an insurer in circumstances where the policy provides for such duty and a claim or claims are advanced in a pleading which, if true, might arguably amount to an occurrence for which there is coverage under the provisions of the policy. Only the policy and the "true nature" of the claims in the

pleading are considered by the court in determining whether a duty to defend has been triggered. See: *Nichols v. American Home Assurance Company*, [1990] 1 S.C.R. 801 (S.C.C.); *Non-Marine Underwriters, Lloyd's of London v. Scalera*, [2000] 1 S.C.R. 551 (S.C.C.); *Monenco Ltd. v. Commonwealth Insurance Co.*, [2001] 2 S.C.R. 699 (S.C.C.); *Cooper v. Farmers' Mutual Insurance Co.* (2002), 59 O.R. (3d) 417 (C.A.); *Halifax Insurance Co. of Canada v. Innopex Ltd.* (2004), 72 O.R. (3d) 522 (C.A.).

[118] Based on the principles established in the duty to defend cases, the Plaintiffs submit that the Defendants' duty to advance defence costs under the Policies is triggered in this case having regard to the claims advanced in the Complaint and that such claims, if true, "arguably" amount to a Wrongful Act for which there is coverage under one or other of the Policies.

[119] American Home submits that, at best, the duty to defend cases are of limited assistance in determining whether a duty to advance defence costs has been triggered under a policy. It points to *Continental Insurance Co. v. Dia Met Minerals Ltd.* (1996), 20 B.C.L.R. (3d) 331 (B.C.C.A.) where the British Columbia Court of Appeal, in the circumstances of that case, held that the pleadings alone should not govern the apportionment of defence costs.

[120] *Dia Met, supra*, involved consideration of the extent of an insurers' obligation to pay the insureds' defence costs under a directors and officers liability policy where the policy required the insurers, among other things, to "defend any suit against the officers and directors

seeking loss payable under the terms of this policy.” The policy did not give the insurer the right to appoint counsel.

[121] The officers and directors of Dia Met were sued and some, but not all of the claims advanced in the action against them related to acts done in their capacity as directors and officers of Dia Met. The insured retained their own counsel. The insurers initially offered to provide counsel of their choice to the insured subject to a reservation of rights. The insured refused. In a subsequent proceeding, the British Columbia Supreme Court decided, pursuant to the provisions of the policy, that the insured retained their rights to control the defence. The issue remained, however, as to what portion of the defence costs the insurers were required to pay given that some of the claims asserted in the action were outside the scope of coverage of the policy. On a subsequent motion for directions, the Chambers judge, after noting that it was impossible to proportion costs with any accuracy in the absence of a final determination of the action, applied an arbitrary allocation as submitted by the insurer.

[122] In allowing the appeal, Newbury J.A. noted the “almost insurmountable difficulty of apportioning defence costs, on the basis of pleadings alone, before or even after trial.” She held that the obligation to indemnify in respect of defence costs should be assessed retrospectively and ordered the insured to provide the insurers with sufficient information to enable the apportionment of the costs, the action having settled prior to the appeal being heard.

[123] In my view, *Dia Met* is very different from this case both in terms of its facts and the issue it was dealing with. What is particularly important is that the insurance policy in issue

in *Dia Met* was very different in respect of the duty to pay defence costs than the Policies in issue here. As I read the decision, the policy in *Dia Met* was a duty to defend policy where, because of an absence in the policy of a waiver by the insured of their right to select and instruct counsel and the actions of the insured in retaining their own counsel, the court held the insurer was obligated to indemnify the insured's defence costs.

[124] It is clear that there is a distinction between the duty to defend and the duty to indemnify in insurance policies. The former is broader than the latter and depends on the nature of the claim, not on the judgment that results from the claim: *Nichols*, supra, at para. 17. It follows, therefore, that where a policy provides that the obligation to pay defence costs is part of the duty to indemnify and nothing more, it is appropriate to assess such costs retrospectively, as was held in *Dia Met*.

[125] That, however, is not the case with the Policies in issue here. The Policies clearly state that American Home assumes no duty to defend. While the obligation to pay defence costs is part of the indemnity language of the Policies, the provisions of the Policies clearly provide that American Home has mandatory duty to advance defence costs, excess of the applicable retention, pursuant to the terms of the Policies, prior to the final disposition of a claim. Clause 8 provides that the Insurer "shall advance". The amounts advanced are referred to as "advance payments." Clause 8 further provides that to the extent and in the event that the Insured is not entitled under the Policy to such payment (i.e. for claims not covered), they are obligated to

repay American Home such defence costs advanced. Finally, Clause 8 provides for an allocation where defence costs are jointly incurred with other companies or individuals.

[126] Based on the clear and unambiguous wording of the Policies in issue dealing with the obligation to pay defence costs, in my view the duty to advance defence costs in the Policies is broader than the duty to indemnify and accordingly because it arises prior to a final determination of the issues in the action, any determination of whether such duty arises must be based on the claim advanced, similar to the duty to defend. What are "covered Defence Costs" can only be determined based on the claims being asserted in the action.

Which Policy applies in respect of the Kipperman Action, the 2002-2003 D&O Policy or the 2004-2005 D&O Policy?

[127] Paragraph 7(c) of the Onex D&O Policies states in relevant part as follows:

(c) If during the Policy Period ... an Organization or an Insured shall become aware of any circumstances which may reasonably be expected to give rise to a Claim being made against an Insured and shall give written notice to the Insurer of the circumstances, the Wrongful Act allegations anticipated and the reasons for anticipating such a Claim, with full particulars as to dates, persons and entities involved, then a Claim which is subsequently made against such Insured and reported to the Insurer alleging, arising out of, based upon or attributable to such circumstances or alleging any Wrongful Act which is the same as or related to any Wrongful Act alleged or contained in such circumstances, shall be considered made at the time such notice of such circumstances was given.

[128] The Plaintiffs submit that the forwarding of the complaint in the Kipperman Action to American Home on July 4, 2005, during the currency of the 2004-2005 D&O Policy

constitutes notice of a Claim under that Policy and accordingly the 2004-2005 D&O Policy applies. The Defendants, on the other hand, submit that the Foley Letter which was sent to American Home on behalf of the Plaintiffs during the currency of the 2002-2003 Onex Policy constitutes sufficient notice of circumstances which may reasonably be expected to give rise to a "Claim" as provided in clause 7(c) of that Policy such that it applies to the Kipperman Action.

[129] Paragraph 7(c) of the 2002-2003 D&O Policy is clear and unambiguous in its wording. It operates to extend the "claims-made and reported" nature of the Policy by providing coverage for a Claim made after the policy period where "circumstances which may reasonably be expected to give rise to a Claim" have been reported to American Home during the policy period.

[130] Such a provision is not unusual in claims made directors and officers' policies. In the publication: *Insurance Law in Canada*, (Toronto: Carswell, 1999) at p. 18-164.5, para. 18.15(j)(iv), Professor Craig Brown states:

D&O policies usually permit, but do not require the report of circumstances that may lead to a claim. The clause may stipulate the type of information that is to be reported. Where such a report is made in accordance with the policy terms, any subsequent claim arising out of the reported circumstances is deemed to have occurred at the time the notice was given.

This is a very valuable coverage for the directors and officers, particularly where the policy is due to be terminated by reason of non-renewal, cancellation, or insolvency. In the absence of such a clause, there would be no coverage where the insured learned of circumstances that could lead to a claim, but where the claim was not made until after termination of the insurance. Coverage may be preserved by giving the appropriate notice pursuant to this clause.

[131] American Home and the Excess Insurers submit that the Foley Letter, sent by Aon to American Home on November 28, 2003 constitutes notice of circumstances pursuant to paragraph 7(c) of the 2002-2003 D&O Policy resulting in the subsequent Kipperman Action being a Claim made during the period of the 2002-2003 D&O Policy.

[132] The Plaintiffs submit that the Foley Letter does not constitute notice of circumstances under paragraph 7(c) of the 2002-2003 D&O Policy because the Foley Letter did not comply with the requirements of 7(c) because it did not contain the specified particulars.

[133] In support of the issue of whether the Foley Letter constitutes notice of circumstances under paragraph 7(c) of the 2002-2003 D&O Policy, the Excess Insurers have filed the affidavit of Geoffrey Raicht, a partner with the law firm of McDermott Will & Emery LLP in New York City. Mr. Raicht has extensive experience in U.S. bankruptcy and insolvency proceedings and he is tendered as an expert in the area. His affidavit attaches a report which provides a basic overview of the structure of U.S. bankruptcy law relevant to the Action; provides a delineation of the developments in Magnatrax's Chapter 11 proceedings, including the progression of procedural steps which occurred as obtained from the US Bankruptcy Court files; and provides a comparison of the entities and causes of action as contained in the Foley Letter and the Kipperman Action.

[134] Based on Mr. Raicht's education and experience, I have no hesitation in accepting his expertise and his evidence concerning US bankruptcy law and the steps which took place in Magnatrax's Chapter 11 proceedings. I am not, however, prepared to consider or

rely on his comparison of the entities and claims asserted in the Foley Letter and the Kipperman Action. In my view Mr. Reich's evidence on the issue of the factual similarities between the Foley Letter and the claims in the Kipperman Action is neither admissible nor helpful. It is an issue that can be determined by me having regard to the documents themselves.

[135] There is no Canadian authority directly dealing with the issue of what constitutes sufficient notice of circumstances under a directors and officers' liability policy to entitle a subsequent claim arising out of such notice to be deemed to have occurred during the policy period. There are, however, a number of American authorities which have considered the issue in the context of directors and officers liability policies. These authorities are relied upon by both the Plaintiffs and the Defendants. While such authority is not binding on me, it is of assistance in determining the issue of whether the Foley Letter constitutes sufficient notice under paragraph 7(c) of the 2002-2003 Onex Policy.

[136] Having said that, I am in agreement with the US cases which hold that in determining whether notice by an insured to an insurer is sufficient, an objective test should be applied having regard to the wording of the policy. The test is whether the insured objectively complied with the notice provision in the Policy: *Continental Ins. Co. v. Superior Court* 37 Cal. App. 4<sup>th</sup> 69 (1995), California Court of Appeal, Second District, Division 3; *McCullough v. Fidelity & Deposit Co.* 2 F3d 110 (1993), Court of Appeal, Fifth Circuit

[137] In my view, the wording of paragraph 7(c) of the 2002-2003 Onex Policy is clear. In order for a Claim made after the policy period to be covered under the 2002-2003 Onex

Policy, Onex must provide written notice to American Home during the Policy Period of the following:

1. circumstances which may reasonably be expected to give rise to a claim being made against a director or officer of Onex;
2. the Wrongful Act allegations anticipated; and
3. the reasons for anticipating a Claim, with full particulars as to dates, persons and entities involved.

[138] In addition, clause 7(c) further requires that the Claim which is subsequently made and reported to American Home must be the same as or related to any Wrongful Act contained or alleged in the notice.

*Timing of the Notice*

[139] There is no issue that the Foley Letter was provided to American Home on November 28, 2003, within the Policy Period of the 2002-2003 Onex D&O Policy.

*Circumstances Which May Reasonably Be Expected to Give Rise To A Claim*

[140] In my view, the Foley Letter set out the circumstances which may reasonably be expected to give rise to a claim being made against a director or officer of Onex.

[141] The Foley Letter was forwarded to American Home by Aon with the latter noting that it contains information which could in the future give rise to a claim. The Foley

Letter, written on behalf of the Creditors' Committee in the Magnatrax Bankruptcy, refers to claims by Magnatrax and its subsidiaries against "parties involved in the May 1999, September 1999 and March 2000 transactions, as well as credit facilities and related agreements supporting those transactions." It further asserts claims related to the "Restructuring and Lockup Agreement." It is clear that those transactions and Agreement involved Magnatrax and the other entities and individuals named in the letter.

[142] Further, the Foley Letter specifically lists the "numerous claims" that the Creditors' Committee alleges exist and lists the entities, including Onex, and the individuals, including the officers and directors of Onex, against whom the claims should be pursued.

[143] Finally, the Foley Letter makes it clear that in the absence of Magnatrax and its subsidiaries prosecuting all of the claims listed against all of the entities and individuals listed in the Letter, the Creditors' Committee will do so.

### *The Wrongful Acts*

[144] In my view, the Foley Letter also clearly lists the Wrongful Acts complained of.

[145] The Foley Letter states that the claims to be asserted include fraudulent transfers, breach of fiduciary duty, aiding and abetting both breach of fiduciary duties and fraudulent transfers, equitable subordination, unjust enrichment, declaratory relief, preference actions and other claims to be identified and that the parties against whom some or all of the claims should be pursued include Onex and its affiliates and officers and directors of Onex.

*The Reasons For Anticipating A Claim With Full Particulars*

[146] The Foley Letter clearly sets forth, in my view, both on its face and in its content, the reasons why Onex and its directors and officers should anticipate a Claim.

[147] Rather than a notice from the insured, the Foley Letter is a lawyers' letter written by a lawyer acting for the Creditors' Committee who is opposite in interest to Magnatrax and Onex.

[148] Further, it clearly indicates an intention to pursue the claim. It requests "immediate" confirmation from Magnatrax that it will prosecute the claims set out in the letter against the entities noted which includes the officers and directors of Onex. It then goes on to state that in the event Magnatrax does not intend to fully prosecute such claims, the Creditors' Committee requests Magnatrax's "immediate" confirmation that the Creditors' Committee can pursue such claims on Magnatrax's behalf. As Mr. Reicht points out in his report, such a request is a necessary step in U.S. bankruptcy proceedings in order for the Creditors Committee to subsequently obtain derivative standing from the U.S. Bankruptcy Court to assert such claims.

[149] The Plaintiffs submit that the Foley Letter does not satisfy the specificity requirements of clause 7(c) of the 2002-2003 D&O Policy in that it does not set out full particulars as to dates, persons and entities involved. In particular they submit that Onex did not describe the nature of the commercial transactions or its role in them; did not specify a single wrongful act they thought might be alleged against them; provided no particulars as to the dates,

persons or entities involved or the names of the directors and officers that had anything to do with Magnatrax.

[150] In my view, when viewed as a whole, the Foley Letter contains sufficient particulars to meet the requirements of clause 7(c). As noted it sets out the specific transactions and agreement involved, the dates of the transactions, the claims which are alleged to exist and the entities and individuals involved. Clause 7(c) contains no requirement to set out Onex's roll in the transactions. While the Foley Letter does not list the individual officers and directors of Onex by name, it does refer to them generally. In my view, that is sufficient, particularly given that the Foley Letter was written by a third party and not Onex. It is not reasonable in the circumstances to require Onex to list the specific names of its directors and officers that the Creditors' Committee may or may not proceed against.

[151] In support of their argument that the Foley Letter is deficient, the Plaintiffs submit that at the time it was sent to American Home, they had more information than was in the notice. As noted, the Foley Letter was sent to Aon in August 2003 shortly after it was received by Magnatrax and Onex but for reasons not explained in the evidence, it was not sent to American Home until November 28, 2003, the eve of the expiry of the 2002-2003 D&O Policy.

[152] The Defendants counter by submitting that the Plaintiffs should not be entitled to rely on Onex's failure to provide sufficient detail to American Home at the time it sent the

Foley Letter or on its subsequent failure to provide additional information concerning the claims as was requested by the American Home.

[153] While there is no direct evidence before me that Onex had more information about the Creditors' Committee's claim than contained in the Foley Letter when it was sent to American Home, it is likely that is the case given Onex's involvement in the negotiations and subsequent agreement to the Magnatrx Plan of Reorganization in the US bankruptcy proceedings. In my view, however, the fact that Onex may have had more knowledge about the claims than was in the Foley Letter at the time it was submitted to American Home or thereafter does not impact on the issue of whether the Foley Letter complies with clause 7(c) of the Policy. As noted, the test is an objective one having regard to the wording of the Policy. What is relevant is the information contained in the notice. As a result, it is immaterial whether the Plaintiffs were in possession of more information than was supplied to American Home. See: *Continental Ins. Co. v. Metro-Goldwyn-Mayer, Inc.* 107F.3d 1344.

[154] The Defendants further submit that based on the testimony of the Aon representatives on the motions, it is clear that when Aon provided the Foley Letter to American Home on November 28, 2003, it was intended as "notice of circumstances" under clause 7(c) of the 2002-2003 D&O Policy.

[155] Once again, because the test as to whether the Foley Letter complies with the provisions of clause 7(c) of the 2002-2003 D&O Policy is an objective one, based on the wording of the Policy, the "intention" of Onex or its representatives is not relevant. The

sufficiency of the Foley Letter must be considered objectively having regard to the wording of clause 7(c).

[156] For the above reasons, therefore, it is my view that the Foley Letter, when viewed objectively as a whole, contains sufficient particulars of the dates, persons and entities involved to comply with clause 7(c) of the 2002-2003 D&O Policy.

***The Claims in the Kipperman Action Must Be The Same or Related to the Wrongful Acts alleged in the Notice***

[157] In my view, it is clear from a review of the Foley Letter and the complaint in the Kipperman Action that the claims being advanced in the Kipperman Action are “the same as or related to” the claims asserted in the Foley Letter.

[158] The Foley Letter referred to claims arising out of transactions in May 1999, September 1999 and March 2000. The Kipperman Action is based on the acquisition of American Building Company by Magnatrx in May 1999, the acquisition of Republic Builders Products in August 1999 and the acquisition of Janock, Ltd. in March 2000.

[159] Further, the claims asserted in the Kipperman Action against the individual Plaintiffs are breach of fiduciary duty; aiding and abetting breach of fiduciary duty; civil conspiracy; and unjust enrichment. The Foley Letter sets out a number of claims including breach of fiduciary duty, aiding and abetting breach of fiduciary duty and unjust enrichment. It is clear, therefore, that the Foley Letter alleges the same or related claims against Onex and its directors and officers that are alleged in the Kipperman Action.

[160] Nor does any issue arise from the fact that the Foley Letter was sent on behalf of the Creditors Committee and the Kipperman Action is brought by the Trustee on behalf of the Litigation Trust. The Litigation Trust was created as part of the Magnatrx Plan of Reorganization in the US bankruptcy proceedings in order to advance the claims alleged by the Creditors Committee against the defendants in the Kipperman Action for the benefit of the creditors of Magnatrx and its subsidiaries.

[161] For the above reasons, therefore, it is my view that the Foley Letter clearly meets the requirements of clause 7(c) of the 2002-2003 Onex Policy such that the Kipperman Action constitutes a Claim made during Policy Period of the 2002-2003 Onex Policy.

Do any of the Exclusions or Limitations of the 2002-2003 D&O Policy and/or the 2004-2005 D&O Policy Operate to Exclude coverage of the Kipperman Action?

a) 2004-2005 D&O Policy

[162] Clause 4 of both the 2002-2003 D&O Policy and the 2004-2005 D&O Policy sets out the exclusions from the Policies. Specifically, clause 4(d) provides as follows:

4. EXCLUSIONS

The Insurer shall not be liable to make any payment for Loss in connection with any Claim made against an Insured:

- (d) Alleging, arising out of, based upon or attributable to the facts alleged, or to the same or related Wrongful Acts alleged or contained in any Claim which has been reported, or in any circumstances of which notice has been given, under any policy of which this policy is a renewal or replacement or which it may succeed in time;

[163] Recognising that exclusions are construed narrowly, in my view, the wording of clause 4(d) is clear and straightforward. Claims covered by prior D&O Policies are excluded from coverage under the current D&O Policy.

[164] As I have already found, based on the notice provided to American Home by the Foley Letter on November 28, 2003, the claims in the Kipperman Action are claims made during the currency of the 2002-2003 D&O Policy in accordance with the provisions of clause 7(c) thereof. The 2004-2005 D&O Policy is a renewal of the 2003-2004 D&O Policy which is, in turn, a renewal of the 2002-2003 D&O Policy. While, therefore, the 2004-2005 D&O Policy is not a direct renewal of the 2002-2003 D&O Policy, it certainly succeeds it in time.

[165] In my view, therefore, Exclusion 4(d) of the 2004-2005 D&O Policy operates to exclude American Home from having to pay for any Loss in connection with the Kipperman Action. It follows that, because the Excess Insurers agreed to follow the form of the American Home 2004-2005 D&O Policy, they are also excluded from any liability under the excess policies for any Loss in respect of the Kipperman Action. The Action should be dismissed against them.

b) 2002-2003 D&O Policy

[166] American Home submits that based on the wording of Endorsement #14 of the 2002-2003 D&O Policy, the specific entity exclusion in respect of Magnatrax, it is not liable

under the 2002-2003 D&O Policy for any Loss arising out of the Kipperman Action.

[167] Endorsement #14 was added the 2002-2003 D&O Policy at the time of the inception of the Magnatrax Run-Off Policy on May 12, 2003. It is entitled: Specific Entity/Subsidiary Exclusion (Claims brought by or against it). It reads as follows:

In consideration of the premium charged, it is hereby understood and agreed that the **Insurer** shall not be liable for **Loss** alleging, arising out of, based upon or attributable to or in connection with any **Claim** brought by or made against the **Entity** listed below and/or any **Insureds** thereof.

1. MAGNATRAX Corporation (including any subsidiary or affiliate thereof)

It is further understood and agreed that the Definition of Subsidiary shall not include MAGNATRAX Corporation. Further, the Insurer shall not be liable to make any payment for Loss in connection with any Claim made against an insured alleging, arising out of, based upon or attributable to any breach of duty, act, error or omission of MAGNATRAX Corporation, or any director, officer, member of the board of managers or employee thereof.

[168] Both American Home and the Excess Insurers submit that Endorsement #14 is an "absolute" exclusion clause which provides a total exclusion of all claims related to or involving Magnatrax.

[169] Once again, I am of the view that the wording of Endorsement #14 is clear and unambiguous. While I agree that Exclusion #14, by its wording, is an exclusion provision, I do not agree that it operates as an "absolute" exclusion in respect of all claims against Onex's directors and officers relating to Magnatrax.

[170] The first paragraph of Endorsement #14 relieves the Insurer from liability under the Policy for any Loss arising from, based upon or attributable to or in connection with any Claim brought by or made against Magnatrax and/or any officer, director or employee of Magnatrax. The wording is clear and straightforward. Any Claim brought by Magnatrax and/or its officers and directors against Onex and its directors and officers is excluded. Likewise, any Claim made against Magnatrax and/or its officers and directors is also excluded.

[171] The second paragraph of Endorsement #14 begins by removing Magnatrax from the definition of Subsidiary under the Policy. This effectively reiterates that American Home is relieved from liability under the Policy in respect of Claims against Magnatrax and its officers and directors.

[172] The final sentence of paragraph two of Endorsement #14 further relieves the insurer of liability under the Policy in connection with any Claim made against an Insured (an officer or director of Onex or its listed subsidiaries) "alleging, arising out of, based upon or attributable to any breach of duty, act, error or omission of" Magnatrax or any director, officer, member of the board of managers or employee of Magnatrax.

[173] Accordingly, when read in its entirety, Endorsement #14 operates to remove Magnatrax (and any subsidiary or affiliate) from coverage under the 2002-2003 D&O Policy and exclude any claim against Onex directors and officers by or against Magnatrax or arising out of, based upon or attributable to any act on the part of Magnatrax or its directors and officers. What Endorsement #14 does not exclude, in my view, is any claim by a third party

against Onex's directors and officers in their capacity as such for their wrongful acts in relation to Magnatrax.

[174] Based on the above interpretation of Endorsement #14, it is my view that the Kipperman Action is not excluded from coverage under the 2002-2003 D&O Policy. As has been previously discussed, the Kipperman Action asserts claims against the individual Plaintiffs in their capacity as directors and/or officers of Onex relating to Magnatrax. The claims are not based upon or attributable to any act on the part of Magnatrax or its directors and officers.

[175] Nor is the Kipperman Action brought by Magnatrax. As noted earlier, the Kipperman Action is brought by the Trustee of the Magnatrax Litigation Trust. The Magnatrax Litigation Trust was established pursuant to s. 4.21 of the Magnatrax Plan of Reorganization which was approved by the US Bankruptcy Court in the Magnatrax bankruptcy proceedings. It is clear, however, from both the Foley Letter and the Complaint in the Kipperman Action that the claims being advanced in the Kipperman Action are claims which, up until their assignment to the Litigation Trust pursuant to the Magnatrax Plan of Reorganization, belonged entirely to Magnatrax and its subsidiaries.

[176] The Foley Letter seeks immediate confirmation from Magnatrax and its subsidiaries in bankruptcy that it will pursue the claims identified against the entities and the individuals named, failing which it requested confirmation that the Creditors' Committee could pursue the claims of Magnatrax and its subsidiaries on their behalf.

[177] The Complaint in the Kipperman Action asserts various causes of action against the individual Plaintiffs based on their alleged actions in respect of certain acquisitions by Magnatrax and its subsidiaries in 1999 and 2000 which caused those companies significant damage, resulting in their bankruptcy. The causes of action initially belonged to Magnatrax and its subsidiaries. The entitlement to pursue such causes of action by way of their transfer and assignment to the Magnatrax Litigation Trust in the Magnatrax bankruptcy proceedings is set forth in paragraphs 125 to 130 of the Complaint in the Kipperman Action.

[178] Notwithstanding that the claims which are asserted against Swartz, Govan, Wright and Hilson in the Kipperman Action are derivative claims which initially belonged to Magnatrax and its subsidiaries, in my view, they are not brought by Magnatrax. The exclusion in the first paragraph of Endorsement #14 of the 2002-2003 D&O Policy is clear. It applies to "any Claim brought by..." Magnatrax or any subsidiary or affiliate thereof. While the Kipperman Action asserts claims which originally belonged to Magnatrax and its subsidiaries, it is brought by the Trustee on behalf of the Magnatrax Litigation Trust and not Magnatrax.

[179] As noted earlier, exclusions are to be interpreted narrowly. In the absence of more expansive wording in Endorsement #14 to exclude derivative claims, the words: "any Claim brought by or made against [Magnatrax, its subsidiaries and affiliates]" restrict the application of the exclusion to claims brought by Magnatrax, its subsidiaries and affiliates. As the Kipperman Action is not such a Claim, Endorsement #14 does not exclude it from coverage.

[180] Nor, in my view, can American Home rely on Endorsement #10 of the 2002-2003 D&O Policy which excludes claims against any Insured where the claim is brought in any bankruptcy proceeding by or against an Organization when the claim is brought by, among others, the creditors' committee or trust. Endorsement #14 removed Magnatrax as a subsidiary thereby excluding it from the definition of Organization under the 2002-2003 D&O Policy.

[181] Accordingly, for the above reasons, it is my view that American Home is required to indemnify the individual Plaintiffs for their defence costs in respect of the Kipperman Action pursuant to the provisions of the 2002-2003 D&O Policy.

[182] American Home submits that pursuant to the Magnatrax Run-Off Policy it is only liable for one US \$15 million limit in respect of pre-May 12, 2003 Magnatrax related claims and it has already paid that amount on account of the Kipperman Action pursuant to the Magnatrax Run-Off Policy. In other words, American Home submits that the Plaintiffs are not entitled to double recovery.

[183] In support of its submission, American Home relies on Endorsement #16 of the Magnatrax Run-Off Policy:

In consideration of the premium charged, it is hereby understood and agreed that, with respect to any Claim under this policy for which coverage is provided by one or more other policies issued by the Insurer or any other member of the American International Group (AIG), (or would be provided but for the exhaustion of the limit of liability, the applicability of the retention/deductible amount or coinsurance amount, or the failure of the Insured to submit a notice of Claim) the Limit of Liability provided by

virtue of this policy shall be reduced by the limit of liability provided by said other AIG policy.

[184] Endorsement #16 applies to the Magnatrax Run-Off Policy. It operates to reduce the limit of liability of the Magnatrax Policy Run-Off Policy by the limit of liability of any other American Home or AIG policy that provides coverage for the claim. Although at the time the Magnatrax Run-Off Policy was entered into the parties agreed to add an endorsement to the 2002-2003 D&O Policy providing for non-pyramiding of limits, no such provision was ever added. In the absence of a provision in the 2002-2003 D&O Policy similar to Endorsement #16 in the Magnatrax Run-Off Policy, there is no basis for reducing the amount required to be paid pursuant to that Policy in respect of the Kipperman Action.

[185] As noted, American Home paid the full extent of its liability of US \$15 million under the Magnatrax Run-Off Policy on account of defence costs incurred in the Kipperman Action. Messrs Ammerman and Blackmon, who were directors and officers of Magnatrax received US \$1,118,008.10 on account of their defence costs and the individual Plaintiffs received US \$13,881,991.90 in respect of their defence costs. American Home's liability under the 2002-2003 D&O Policy does not extend to paying the Plaintiffs for defence costs already reimbursed. It does extend, however, to any defence costs incurred by the individual Plaintiffs in respect of their defence of the Kipperman Action.

[186] In reaching my decision that American Home is required to indemnify the individual Plaintiffs in respect of defence costs incurred in the defence of the Kipperman Action pursuant to the 2002-2003 D&O Policy, I wish to make it clear that I have not considered the effect of such decision on the Magnatrax Run-Off Policy, having particular regard to Clause 8 and Endorsement #16 of that Policy and the amounts previously paid to the individual Plaintiffs pursuant to it. Those issues were never raised by the parties on the motions and were not argued before me.

### **Conclusion**

[187] For the reasons set out in the Introduction, on the consent of the parties, the Plaintiffs' summary judgment motion and the Action are dismissed against the Defendants Liberty Mutual Insurance Company and Houston Casualty Company. It follows that the cross-motions of the said defendants are dismissed as well.

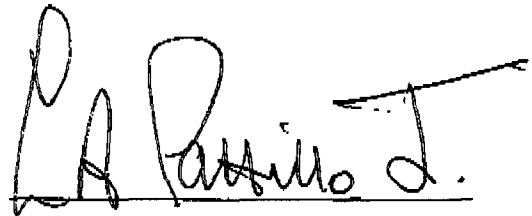
[188] Further, and for the above reasons, the Plaintiffs' summary judgment motion is dismissed against the remaining Excess Insurers, the Defendants Brit Syndicates Ltd. (Lloyd's Syndicate 2987), Heritage Managing Agency Limited (Lloyd's Syndicate 3245) and XL Company Limited and their cross-summary judgment motions are allowed and the Action is dismissed against those Defendants in its entirety.

[189] The Plaintiffs' summary judgment motion is allowed against American Home in accordance with paragraphs (b) of their Amended Notice of Motion dated November 30, 2009 granting the Plaintiffs a declaration that American Home is required by the terms and conditions

of the 2002-2003 D&O Policy to indemnify the plaintiffs as their interests may appear in respect of defence expense incurred and ongoing on behalf of the individual Plaintiffs in defence of the Kipperman Action to the extent that such expenses were not covered under the Magnatrax Run-Off Policy and judgment against American Home consequential to such declaration in an amount to be determined by the court.

[190] American Home's cross-summary judgment motion is dismissed.

[191] In the event that the parties are unable to agree on costs within 30 days from the date of this judgment, they should arrange a conference call through my assistant to agree on a procedure to resolve costs.

A handwritten signature in black ink, appearing to read "L.A. Pattillo J.", written over a horizontal line. The signature is stylized and cursive.

L.A. Pattillo J.

**Released:** June 30, 2011

**CITATION:** Onex v. American Home, 2011 ONSC 1142  
**DATE:** 20110630  
**DOCKET:** CV-08-00365387

**ONTARIO**

**SUPERIOR COURT OF JUSTICE**

**BETWEEN:**

**ONEX CORPORATION, GERALD W. SCHWARTZ, CHRISTOPHER A. GOVAN, MARK HILSON AND NIGEL WRIGHT**

Plaintiffs

- and -

**AMERICAN HOME ASSURANCE COMPANY, BRIT SYNDICATES LTD. (LLOYD'S SYNDICATE 2987) AND HERITAGE MANAGING AGENCY LIMITED (LLOYD'S SYNDICATE 3245), XL INSURANCE COMPANY LIMITED, LIBERTY MUTUAL INSURANCE COMPANY, LLOYD'S UNDERWRITERS SYNDICATES NO. 2623, 0623, 0033 AND AIG EUROPE (UK) LIMITED, HOUSTON CASUALTY COMPANY**

Defendants

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**REASONS FOR JUDGMENT**

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**PATTILLO J.**

**Released: June 30, 2011**